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World Financial Markets

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The dollar: correction or plunge?

In mid-January foreign exchange market sentiment toward the dollar started to undergo a change. From January 11, when it peaked against the European currencies, to March 29, the dollar fell 9% against the German mark, and 5% against the yen (see Table 1). It also weakened 5% against the Swiss franc and 4% vis-à-vis sterling. In contrast, it rose 2% relative to the Canadian dollar. As a result, on a nominal effective basis the dollar dropped 4% (6% if the Canadian dollar is excluded from the effective calculation). The big question now is, Will the dollar continue to fall, and if so, will the fall be gradual and limited — or disorderly and steep?

Among the many explanations for the shift in sentiment toward the dollar, three stand out: concern, which has been underscored by statements from various Washington officials, about the future financing of both the budget deficit and the mounting imbalances in U.S. trade and current accounts; financial market anxieties about rapid economic growth that could trigger an increase in inflation in the uncertain climate of an election year; and some restoration of confidence in the prospects for economic recovery and political stability abroad, notably in Germany. The recent decline in the dollar can be welcomed as a healthy correction from peaks not justified by basic economic considerations. However, if correction is not to turn into something much worse, it is vital that financial markets retain confidence in U.S. noninflationary growth policies.

It is worth recalling the episode of dollar decline in 1977. At the time, the U.S. authorities sought to talk down the dollar in order to stem the current account deficit resulting from faster economic growth in the United States than in other industrial countries. The U.S. economy was into its second year of expansion while others lagged. And the question of how rapidly U.S. inflationary pressures would build was beginning to trouble both foreign and domestic investors in dollar assets. The official welcome for depreciation led to a drastic decline in the dollar that helped ignite U.S. inflation, which in turn could only be arrested through the costly and protracted recession and disinflation of 1980-82.

While today's current account deficit is linked to the dollar's strength since 1981, it does not stem solely from a currency overvalued in terms of purchasing power. No less significant has been the combination of vigorous economic growth at home,

Table 1

Exchange rates

	Mar 29, 1984*	Percent change from Jan 11, 1984**	Percent change from Dec 31, 1983**
Dollar (1980-82=100)			
Nominal effective	115.4	—3.7	—1.5
Real effective	112.3	—4.4	—2.5
Canadian dollar	1.279	+2.1	+2.7
Japanese yen	223.9	—4.5	—3.3
French franc	7.960	—8.4	—4.4
German mark	2.583	—9.1	—5.1
Italian lira	1.616	—5.5	—2.4
Swiss franc	2.142	—4.9	—1.7
Pound sterling	1.450	—3.8	+0.1

*Local currency units per U.S. dollar, except for pound sterling.

**Minus indicates depreciation of the dollar.

Chart 1

U.S. balance of payments

in billions of dollars

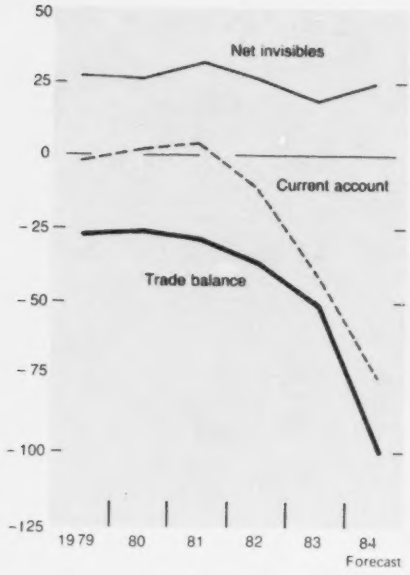
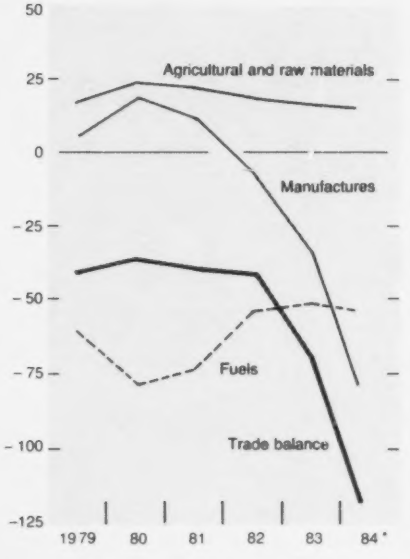


Chart 2

U.S. trade balances by sector

exports f.a.s./imports c.i.f. basis

in billions of dollars



*Jan–Feb at annual rate

prolonged weakness in Europe, and the collapse of export markets in Latin America. Reliance now on a sharp fall in the dollar as the principal means to eliminate the external deficit rapidly would not be in anyone's interest. Not only would U.S. inflation flare up, in time necessitating new restraint and its consequences, but Europe's fledgling recovery might be derailed. Even more important, LDCs would suffer shrinkage in their most important export market and their debt-servicing problems would be seriously aggravated by the rise in dollar interest rates that would certainly ensue.

The basic challenge before governments of industrial countries is to achieve more balanced global economic growth performance. That would permit a significant reduction in the U.S. current account deficit over a period of two to three years. With the proper distribution of exchange rate and growth adjustments worldwide, the depreciation of the dollar could be kept gradual and limited, obviating the need to engineer a sharp depreciation.

The U.S. external financing problem

One reason for dollar weakness is rising concern about the widening U.S. current account deficit, centering on its financing, and what its prolongation implies about the nation's international standing. The exchange markets took note particularly of the warning that the United States is "on the verge of becoming a net debtor internationally," that it could "soon become the largest," and that the stability of the dollar and domestic financial markets could become "hostage to events abroad."

By the official estimate, the U.S. current account deficit amounted to $41 billion in 1983, widening throughout the year to $61 billion at an annual rate in the fourth quarter. The deficit in 1982 was only $11 billion. The main locus of 1983's $30 billion deterioration on current account was a $24 billion jump in the merchandise trade deficit (balance of payments basis) (see Chart 1). On the more familiar customs-CIF valuation the merchandise imbalance exceeded $90 billion in the closing quarter of 1983 and for this past January-February period hit a new record annual rate of $117 billion ($9.8 billion at a monthly rate).

Although the surplus on agricultural trade has held fairly steady since mid-1983 and petroleum imports are roughly at 1982 levels, there is slim evidence as yet that the fast deterioration of the manufactures balance is over (see Chart 2). Some encouragement may perhaps be drawn from the 3% January-February rise in exports over December, principally to Europe, Canada, and Latin America (see Table 2). Export growth will have to continue during the course of 1984 and import growth slow substantially, if the full year's U.S. trade deficit is to be held below $100 billion (balance of payments basis) and the current account deficit below $75 billion (see Table 3).

A deficit of that magnitude is unprecedented for the United States. Still, experience of the ups and downs of the OPEC surplus since 1973 makes the point that payments imbalances that seem severe and intractable are sometimes resolved surprisingly fast. Nonetheless, the prospect of a $75 billion U.S. current account deficit this year, and still more the risk that it might continue unchecked in future years, is troubling from several points of view.

First, some find it improper for the world's wealthiest nation to divest foreign savings to finance domestic consumption higher than

Table 2

U.S. merchandise trade

percent change from year ago

	1983	Jan-Feb 1984
Exports	—5.5	+5.4
Industrial countries	+0.2	+15.0
Canada	+13.4	+34.0
Japan	+4.4	+21.2
Western Europe	—6.8	+0.6
France	—16.2	—4.9
Germany	—5.9	+13.8
Italy	—15.4	—1.6
United Kingdom	—0.2	+9.0
Developing countries	—12.5	—2.7
OPEC members	—26.0	—22.3
*Latin America**	—20.1	+34.8
Imports (CIF)	+5.9	+27.5
Industrial countries	+7.4	+38.8
Canada	+12.3	+38.9
Japan	+9.1	+40.5
Western Europe	+3.0	+36.4
France	+8.4	+100.4
Germany	+5.8	+51.1
Italy	+2.8	+172.8
United Kingdom	—4.7	+20.7
Developing countries	+3.7	+32.8
OPEC members	—19.1	—41.6
*Latin America**	+10.3	+50.4

*Excluding Ecuador and Venezuela.

Table 3

U.S. current account

billions of dollars

	1983	1984*
Merchandise exports	200.2	220.0
Merchandise imports	260.8	320.0
Trade balance	—60.6	—100.0
Net invisibles	19.8	25.0
Current account	—40.8	—75.0

*Forecast.

would be possible in the absence of the current account deficit. Would not LDCs find better use for scarce world savings? Such questions should consider that international investors place capital in the United States for greater or more secure return than they judge attainable elsewhere. Their judgment should not be lightly cast aside. The goal of restoring voluntary private capital flows to LDCs from the United States and other industrial countries will not be reached until LDCs establish an attractive investment climate. The process includes the working down of excessive debt levels, when these have grown out of line with export earnings, and is actually speeded up by vigorous U.S. import demand and the associated U.S. current account deficit.

A second criticism of the U.S. external deficit lies with its implications for the nation's net foreign position. At the end of 1983 the United States enjoyed a net international creditor position, estimated according to Department of Commerce definitions at $125 billion (see Chart 3). If the $75 billion current account deficit expected for 1984 were to persist in 1985 the entire net asset position that the United States has accumulated over the past half century would be wiped out before the end of next year. That conclusion may be premature since it overlooks the statistical inadequacies in the recorded U.S. current account and the nation's external balance sheet, which make no allowance for the world current account discrepancy that now runs at around $100 billion annually.

The discrepancy implies that, around the world, deficits are being overstated or surpluses understated in the reported statistics, principally on service transactions and investment income. Much of the rise in OPEC members' service imports after the second oil shock finds no counterpart in recorded receipts by industrial countries or other LDCs. Moreover, there are contradictions in industrial-country data on capital positions. For example, banks reporting through the BIS listed liabilities to U.S. nonbanks of $87 billion as of June 1983. At that same time, U.S. nonbanks reported to the U.S. authorities claims on foreign banks of only $41 billion, suggesting the possibility of significant understatement of both investment earnings and the net asset position in the official U.S. data.

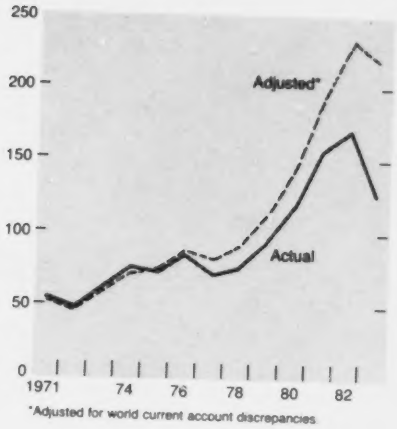
Although no precise calculation can be made, even a conservative allocation of the world current account discrepancy would credit the United States with an additional $25 billion per annum in recent years. Thus the adjusted net creditor position of the United States may not be as close to exhaustion as recent statements have proclaimed (see Chart 3). Both its level and rate of erosion are actually much in doubt. Still, any deterioration gradually undermines the structural strength in net investment earnings that the United States has attained in recent years.

A shift by the United States to a net debtor position need not be destabilizing for the dollar. The net position has no necessary bearing on the ease with which the current account deficit can be financed, since there is no reason to assume that domestic holders of dollar assets behave very differently from foreign holders. The fact that the United States was a net external creditor in the late 1970s did not prevent a sharp depreciation of the dollar when investors' confidence in U.S. macroeconomic policies failed. There was ominous talk of a dollar overhang in official reserve portfolios. An elaborate scheme was advanced for an IMF substitution account that would forestall diversification of reserves out of dollars, alleged at the time to

Chart 3

U.S. net asset position

in billions of dollars



*Adjusted for world current account discrepancies

Table 4

U.S. balance of payments

billions of dollars
minus sign indicates an outflow

	1982	1983
Current account balance	—11.2	—40.8
Changes in U.S. holdings of foreign assets	—118.0	—49.3
Official holdings	—10.7	—6.1
Private holdings	—107.3	—43.2
Direct investment	3.0	—7.6
Claims of U.S. banks	—109.3	—25.0
Changes in foreign holdings of U.S. assets	87.9	83.0
Official holdings	3.2	6.1
Liabilities of U.S. banks	—2.1	0.9
Private holdings	84.7	76.9
Direct investment	10.4	9.5
U.S. Treasury securities	7.0	8.6
Other U.S. securities	6.1	8.6
Liabilities of U.S. banks	64.3	51.3
Statistical discrepancy	41.3	7.1

be a key source of currency instability. The main lesson from the 1970s' debacle is that investors — official or private, domestic or foreign — will attempt to move their portfolios into currencies other than the dollar if they judge that the real value of their wealth will be eroded by inflationary U.S. policies or that better returns can be obtained abroad. Thus the future of the dollar is very much a question of confidence.

Provided confidence is well maintained, the financing requirements of large current account deficits need not precipitate a drastic fall in the dollar. In 1983, investor confidence was so strong as to drive up the dollar, suggesting, on an *ex ante* basis, that investors desired to place more funds in dollar assets than were needed to finance the current account deficit. As things turned out, according to official balance of payments accounts, there was no need for increased foreign capital inflows into the United States last year because the increase in the current account deficit from $11 billion in 1982 to $41 billion in 1983 was more than covered by a substantial decline in U.S. capital outflows (see Table 4). That decline also made up for a large drop in net unrecorded capital inflows. The shrinkage of the positive errors and omissions item in 1983 suggests a sharp diminution of capital flight from other countries into the United States.

Banks were principally responsible for last year's recorded decline in U.S. capital outflows (see Table 5). There was a slowdown in U.S. banks' lending to LDCs in general (excluding offshore centers) as well as in lending to Europe. The latter reflected slower growth in the interbank market and weaker credit demand due to a lagging economic recovery. At the same time, banks became net capital importers in 1983, a shift that can also be traced partly to the rise in domestic interest rates relative to Eurodollar rates (see Chart 4) which provided an incentive for banks to fund more of their needs in the Euromarkets.

Financing the large and increasing current account deficit in 1984 will not be as easy as in 1983. It can be done, but most likely at higher interest rates. How high a price will be determined by the level of investor confidence. While a sharp drop in the dollar, as advocated by some, might reduce the current account deficit more quickly, it could make the financing of the current account deficit more difficult by undermining investor confidence. This could lead to considerable pressures on the dollar, which would raise prices and prompt much higher interest rates. To forestall such a course of events and to secure financing of the current account deficit in an orderly manner with minimum risk of sharp increases in domestic interest rates, the issue of the domestic policy mix has to be addressed.

U.S. inflation on the rise?

At the beginning of 1983 the financial community shared Administration hopes for a gradual U.S. economic recovery that would avoid overheating and accelerating inflation. Actual performance during 1983 broadly played by the script. Real GNP growth trended down from a peak 9.7% in the second quarter to 5% in the fourth, and it seemed that the economy was settling into a steady trot. Moreover, although consumer price inflation edged up after midyear from its recession trough, it seemed to hold at a 5% annual rate thereafter.

Events in 1984, however, cannot be reassuring to proponents of a sustainable and noninflationary course. Confounding both market and official expectation, U.S. real GNP growth bounced up to an ini-

Table 5

Banks in the U.S.: own claims on and liabilities to foreigners

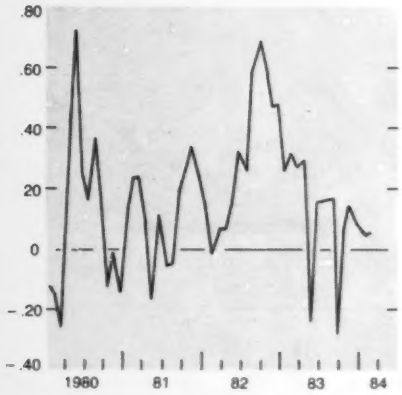
end-December
Billions of dollars

	1982	1983
Claims on		
Own foreign offices	127.3	143.9
Unaffiliated foreign banks	121.4	120.9
All others	107.0	119.6
Total	355.7	384.4
Liabilities to		
Own foreign offices	119.2	147.4
Unaffiliated foreign banks	50.2	59.6
All others	57.6	74.0
Total	227.1	281.0
Net claims on		
Own foreign offices	8.1	—3.5
Unaffiliated foreign banks	71.1	61.3
All others	49.4	45.6
Total	128.6	103.4

Chart 4

3-month interest rate differentials

$ LIBOR minus domestic CDs *



tially estimated 7.2% in the first quarter. Since mid-1983, domestic demand has been growing even more rapidly but not all of this strength shows in the output and GNP figures because it has been satisfied increasingly through higher imports. It is interesting to recall the experience of the late 1970s. Charts 5 through 8 compare the current recovery with the one starting in 1975. Real GNP, employment, and industrial production are now increasing just as rapidly, if not more so, than in the earlier recovery. And while the inflation cycle is beginning from a lower base this time, it seems to be following roughly the same pattern as before.

Most mainstream forecasters take comfort from the still-sluggish wage figures for the economy at large and believe that memories of the severity of the employment shakeout during the 1980-82 recession will linger for some time to come. But with a rapidly tightening labor market (the unemployment rate has fallen to 7.8% from its peak of 10.7%), briskly rising capacity utilization (now above 80%), and sparkling corporate profits, price and wage pressures are likely to become stronger. Furthermore, commodity prices are also increasing. Measured by *The Economist* dollar index they are up 30% from their 1982 low and 3% in just the first three months of 1984. Also, short-term business credit in March is estimated to be 4% higher than three months ago. The standard inflation forecasts of 5%-6% from the fourth quarter of 1983 to the fourth quarter of 1984 could quickly change to 6%-7%, particularly if there is substantial downward correction of the dollar.

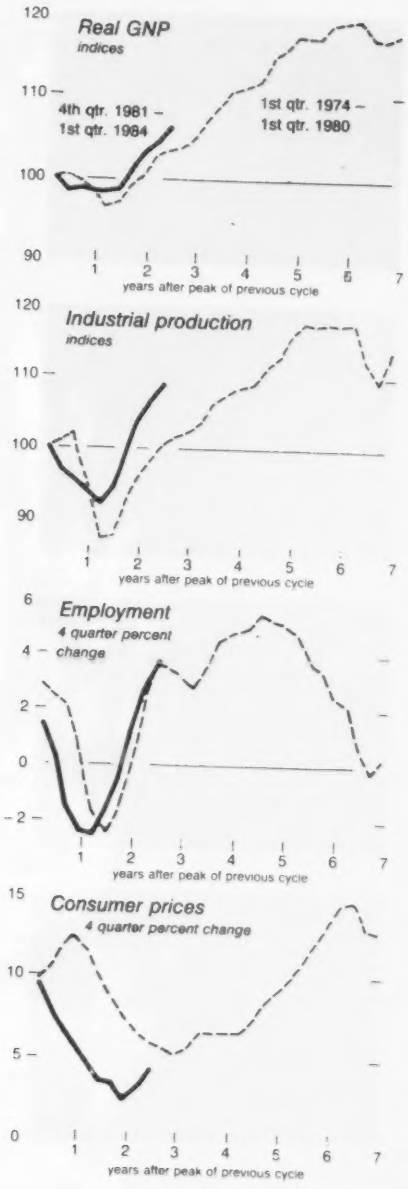
If previous experience has any message for today, it must be that an expansion of domestic demand on the order of 8% at an annual rate is not sustainable. If the rate of growth does not slacken, as a few analysts suggest it will soon, some policy restraint is needed to help moderate it. There is near-unanimity that fiscal correction is a tool far superior to monetary restriction as the way to brake the potentially runaway U.S. economy, the more so as the trade deficit widens. In the domestic context, reliance on monetary restraint imposes disproportionate burdens on such sensitive sectors as housing, autos, and consumer durables. It also poses financial risks for companies that are highly leveraged, especially those with large short-term or floating-rate liabilities taken on during the last recession. Moreover, for any given curtailment of overall domestic growth, a slowdown achieved through monetary restraint provides less benefit to the trade balance than does one reached by fiscal discipline. By slowing or even preventing correction of the dollar, a monetary squeeze is prone to delay recovery of U.S. competitiveness in markets at home and abroad. Sharp increases in U.S. interest rates also could set back recovery of U.S. export markets, especially in debt-burdened LDCs.

Better understanding of these disadvantages of monetary restriction has helped impart momentum to the President's proposal that steps be taken this year to implement a phased reduction of the federal budget deficit. The imperative for the United States to begin a resolute shift toward fiscal restraint is reinforced by the fact that U.S. willingness to take that step has become the litmus test for sustained investor confidence in U.S. economic management. Without fiscal constraint the markets judge that the Federal Reserve would be obliged to monetize the budget deficit at some point as the economy moves to full employment, rather than letting interest rates rise without limit.

The Administration's last-published forecast for FY 1984's budget deficit

Charts 5–8

Economic recoveries



is $184 billion, compared with the $195 billion outcome for FY 1983. The strength of the economy may help reduce the deficit to $175 billion this year. For the medium term, according to the Congressional Budget Office, the Administration's January budget proposal still leaves deficits — largely structural in nature — of around $185 billion in each of the fiscal years 1985-88.

The President and Senate Republicans are now proposing a down-payment package that maintains the overall supply-side orientation of the President's program but could reduce the cumulative deficit by $150 billion over FY 1985-87 through roughly equal amounts in reduced military spending, cutbacks in other domestic spending, and increased taxes. House Democrats have another proposal that cuts the deficit by about $30 billion more over the three-year period. Here, aggregate tax increases are of the same magnitude as in the President's package but military spending is reduced by twice as much while social-spending cuts are half as large. This package also incorporates a pay-as-you-go provision that matches future spending increases with a rise in taxes. Other plans combine various features of these packages and cut the deficit by even larger amounts through lower spending, higher taxes, and some deferment of tax indexation. Most of these plans cut military spending more than the President's. The political focus at this stage is still on the philosophical mix to be combined in the package. A compromise package, it would appear, is still some time away from enactment.

These deficit-reducing efforts are a very welcome development, but they would result in no more than a down payment toward the long-term goal of the gradual elimination of the structural deficit. The Congressional Budget Office estimates that the President's plan would reduce the deficit by a cumulative total of only $100 billion spread over the next three years. Moreover, most of the cuts, as currently proposed, would occur toward the end of the FY 1985-87 period. This back-end loading of the deficit reduction would leave the United States with a fiscal policy that is still procyclical, even though the economy is already moving toward full employment.

There should be no misapprehension that progress on the fiscal deficit will permit relaxation of U.S. monetary policy. While the economy still was operating far below capacity it could not do much harm for the Federal Reserve to err on the side of ease in forming its judgments on desirable money growth and the associated level of bank reserves and interest rates. That leeway now is gone. With economic growth so much more rapid than anticipated it is little comfort that the money aggregates are currently within their target ranges. Those ranges cannot stand in sacrosanct isolation when there is clear risk to the fundamental goal of sustained, noninflationary growth. Nor can the Fed know with any precision the consequences of a given level of interest rates or rate of money growth given the vagaries of velocity. Because of the market's acute sensitivity to any hint of policy indecision, the Federal Reserve must set a prudent course that errs, if at all, on the side of restraint.

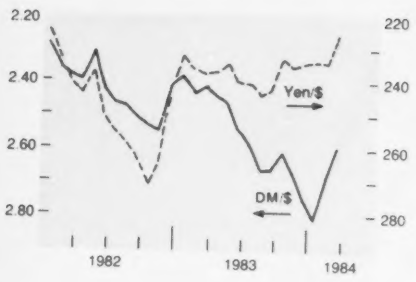
European recovery strengthens

While concern over the U.S. financing and inflation outlook may have been the principal source of the change in sentiment toward the dollar this year, there has also been some reassessment by the markets of Europe's political and economic prospects. The dollar's surprising strength late in 1983 occurred main-

Chart 9

Spot exchange rates

monthly averages



ly vis-à-vis European currencies (see Chart 9). Their weakness was accentuated by perceptions of a general European malaise, with fears of political turmoil from the installation of Pershing missiles and pessimistic readings of Germany's economic outlook. Although longer-term worries continue about Europe's political and economic cohesion and its technological competitiveness, the neutralist tendencies in Germany have been contained for the time being and German economic performance is turning out quite strong. With these clouds over Europe seeming to have lifted a little, an upward correction of European currencies against the dollar was in order. Notwithstanding a widening interest-rate differential in favor of the dollar, underlying asset preferences now embody increasingly positive views of Europe. Evidence of this can be seen in the continuing strength of European stock markets this year in contrast with weakness in U.S. markets.

Until late 1983 there was concern about Germany's ability to achieve even 2% growth in 1984. By the end of 1983, it turns out, real GNP was actually back to its highest point in over three years, equal indeed to the peak level reached in the first quarter of 1980. Updated projections now call for slightly more than 3% growth in 1984, a major improvement on the 1.3% achieved last year.

Better export prospects have greatly brightened business sentiment in Germany. Export growth was below 3% in the first half of 1983, partly due to the dramatic cutback in French imports under the austerity program. By year-end German exports were rising at annual rates of over 10%. Exports to the United States soared in the second half of 1983, and were up nearly 40% in dollar terms by December from a year earlier. The share of sales to the United States in all German exports increased to 9.3% in December from 6.6% in December 1982. The increase in exports to the United States directly and indirectly contributed up to half of Germany's overall 1.3% rise in real GNP last year.

The improved economic climate in Germany heightens the likelihood of further dollar decline against the mark. With sustained economic growth now established, the German authorities will be reluctant to resist mark appreciation by letting domestic interest rates drop. Large increases in money supply would be unwelcome. Nor are lower interest rates appropriate if high real wage increases give a further boost to domestic demand.

The U.K. recovery is proceeding at a steady pace. Real GDP is expected to rise about 2.5%-3% this year, following a similar rise in 1983. A striking fall in Britain's personal savings rate, coupled with rising real earnings for those employed, has provided sustained strength to U.K. private consumption. Much of the increase in final demand has been met by imports. However, it does at last appear that U.K. industrial production is on the rise — even in manufacturing. Although there are tentative signs of an upturn in private-sector wages, inflation remains at about 5%. U.K. investment intentions are now quite positive, and business confidence has plainly improved.

Despite these constructive features, sterling has gained little on the dollar and has weakened considerably against the mark this year. Downside risks on oil prices may have contributed. More importantly, U.K. interest rates have recently come down a little in both nominal and real terms. By the latter measure they are now among the lowest in the major countries. These are indications that monetary restraint in Britain is not as tight as a mechanical reading of U.K. money supply

Table 6

Growth and inflation outlook

percent change

	Growth rate*		Consumer prices**	
	1983	*1984*	*1983*	*1984*
United States	3.3	5.7	3.8	5.5
Canada	3.0	4.2	4.5	6.0
Japan	3.2	4.4	1.9	2.2
Western Europe	0.9	1.8	7.9	6.7
France	0.5	0.5	9.3	7.0
Germany	1.3	3.2	2.6	2.6
Italy	—1.7	1.5	12.9	10.0
United Kingdom	3.0	2.7	5.3	6.0

*Real GNP except France, Italy, and the United Kingdom where real GDP is used.

**December-December.

numbers or targets might suggest. Whereas the assertion of macroeconomic control was the government's major preoccupation during its first term, the focus now is more on structural reforms to improve the workings of market forces. The March budget, neutral or slightly expansionary in its implications for demand, introduced bold steps to curtail distortions in the tax system, which have unduly institutionalized saving and favored investment of doubtful productivity. The medium-term benefits of these supply-side reforms could be considerable.

Sustained economic growth in Germany and the United Kingdom, together with expanding export markets in the United States, brightens the economic prospects for the rest of Europe. The rest also gain from the steps they are taking themselves to tackle the structural imbalances portrayed by high inflation and by large government or external deficits. Italy is moving toward reducing wage indexation; Belgium and the Netherlands are devising programs to cut their large public-sector deficits; and France has reduced its current account deficit significantly through the austerity program initiated last year. Although domestic demand remains weak in these countries, because purchasing power is squeezed by falling real wages and higher taxes, their overall output may increase slightly thanks to higher exports. On the whole, European growth should average 1.8% this year, compared with 0.9% in 1983 (see Table 6).

Conclusions

A U.S. current account deficit on the order of $75 billion a year is not sustainable. Still, a rapid elimination would not be desirable as it would have a major deflationary impact on the world economy. In fact, a U.S. deficit of $20 to $30 billion a year in the official figures is entirely reasonable as long as the world current account discrepancy is on the order of $100 billion. For the time being, the financing of a U.S. deficit considerably larger than $20-$30 billion should not pose major problems, since faster U.S. growth will tend to raise U.S. interest rates that attract the requisite capital inflows from abroad.

It would be unwise to attack the current account deficit solely by a large devaluation of the dollar. A strong dollar has important benefits for the U.S. economy. It keeps inflation low and improves cost efficiency. A precipitous decline would be harmful both to the United States and to the rest of the world. Rapid inflation would ensue in the United States, leading to very high dollar interest rates that could precipitate another global recession. Other industrial countries would find their export competitiveness seriously reduced by a sharp fall of the dollar, which would hamper their economic recovery.

Nor would LDCs necessarily benefit from a major decline in the dollar. True, while the dollar was strengthening, LDC debt-servicing capacity was impaired because even an unchanged volume of exports provided a reduced flow of dollar earnings to service debt that was predominantly denominated in dollars. To the extent that dollar strength, related in part to high interest rates, depressed real demand for LDCs' exports, their plight was further aggravated. Symmetry argues that LDC debt-servicing burdens would be alleviated if the dollar now weakens.

However, comfort should not be drawn in haste. It is not clear whether LDCs generally would experience any significant terms-of-trade improvement from a weaker dollar, although oil-importing countries could benefit if oil prices remain stable in

dollar terms. Furthermore, if dollar weakness were to necessitate higher U.S. interest rates, any LDC terms-of-trade gains could be offset, at least in part, by rising interest payments.

The preferable resolution of the U.S. current account deficit is a modest decline in the dollar combined with a better distribution of world economic growth. Reduced fiscal stimulus through a cutback in the federal budget deficit should help slow U.S. growth to sustainable noninflationary levels in the years ahead. It would also maintain the investor confidence necessary to finance the current account deficit. At the same time, faster growth abroad would help lower the U.S. current account deficit and reduce growing surpluses in some large industrial countries. While growth prospects in Europe and Japan now appear somewhat brighter, some policy stimulus is still desirable as unemployment levels, particularly in Europe, are far too high. In countries where fiscal consolidation has cut budget deficits or inflation remains very low, future tax cuts and reforms should be used to stimulate domestic demand. A modest decline in the dollar also should allow a somewhat more accommodative monetary policy in Europe and Japan. With stable to lower interest rates abroad and a modest increase in U.S. interest rates the resulting higher interest rate differentials in favor of the dollar should help moderate its depreciation. A gradual, modest decline of the dollar and more even distribution of growth would benefit all countries, but a sharp drop could subject the world economy to another stagflationary shock.

Statistical appendix

for key to data in tables see pages 18 and 19.

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Information herein is from sources considered to be reliable but is furnished without responsibility on the part of Morgan Guaranty Trust Company.

Nominal effective exchange rates

Index numbers, 1980-82 average = 100. Each index shows a currency's trade-weighted appreciation or depreciation measured against 15 other major currencies, using averages of daily noon spot exchange rates in New York and bilateral trade weights based on 1980 trade in manufactures. Annual figures are calendar year averages.

	United States	Canada	Japan	Australia	France	Germany	Italy	United Kingdom	Austria	Belgium	Neth-erlands	Spain	Swit-zerland	Den-mark	Norway	Swe-den
Pre-June 1970 parities	114.6	114.4	69.0	116.4	111.1	66.2	226.2	147.5	80.6	91.1	82.1	143.2	51.3	113.0	92.3	119.6
Smithsonian central rates	103.1	121.9	77.2	116.7	109.8	68.9	220.9	146.7	80.6	92.3	82.9	142.7	53.2	110.8	90.9	117.6
1980	90.7	100.4	95.5	96.0	106.5	100.0	108.4	99.8	99.4	105.9	100.2	106.5	95.4	105.1	98.2	103.9
1981	99.5	100.2	105.8	104.0	100.4	97.2	98.8	102.1	98.9	101.6	97.1	99.4	98.3	99.2	100.1	103.3
1982	109.8	99.4	98.6	100.1	93.1	102.8	92.8	98.1	101.7	92.3	102.7	94.1	106.3	95.7	101.7	92.8
1983	114.2	100.8	107.8	92.0	87.3	107.6	90.3	91.6	103.6	90.0	105.0	78.4	111.5	96.4	99.4	82.2
1983																
March	112.0	100.9	105.8	89.3	90.8	108.9	91.3	86.4	104.8	92.2	106.5	80.5	108.4	98.7	97.8	81.2
April	112.5	100.4	106.4	87.5	87.7	109.1	91.3	90.2	104.4	91.5	105.1	80.1	109.9	98.7	98.7	81.5
May	112.2	100.6	107.9	88.2	86.8	108.5	90.8	92.9	104.0	90.8	104.8	79.5	110.6	97.5	99.3	81.7
June	114.3	100.8	106.6	89.4	86.4	107.6	90.7	93.6	103.4	90.2	104.6	78.3	110.6	96.2	99.5	82.2
July	115.1	101.0	106.9	89.8	86.2	107.2	90.6	93.4	103.5	89.7	104.5	76.8	111.7	95.4	99.9	82.6
August	117.0	101.2	106.2	91.5	85.6	106.5	89.6	94.0	103.1	89.2	104.1	77.0	112.3	94.5	100.3	82.8
September	116.7	101.3	107.1	92.2	85.6	106.9	88.9	93.8	103.3	88.8	104.2	76.7	112.4	94.9	100.9	82.6
October	114.8	101.0	110.7	93.5	85.4	108.0	88.6	92.2	103.8	88.7	105.0	76.0	113.2	95.2	100.8	82.3
November	116.5	100.9	110.7	94.8	85.1	107.1	88.3	92.8	103.2	88.4	104.4	75.9	112.8	94.6	100.9	82.7
December	118.0	100.4	112.1	94.2	84.7	106.8	88.0	91.8	102.8	88.2	104.1	75.8	113.8	94.0	99.5	83.1
1984																
January	119.1	100.5	113.3	95.5	84.1	106.5	87.6	91.5	102.6	87.7	103.7	76.3	113.8	93.6	99.2	83.4
February	117.3	100.2	111.9	97.3	84.7	108.0	87.0	91.4	103.5	88.3	104.3	77.1	112.2	94.0	99.0	82.9
March 2	115.7	99.5	111.3	96.9	85.3	109.0	86.9	91.8	104.0	88.8	104.9	77.3	111.0	94.4	98.8	83.1
9	114.4	98.5	115.1	96.8	85.4	109.2	87.1	90.1	104.5	89.0	105.2	77.4	112.0	94.7	98.7	83.4
16	115.1	97.7	115.1	98.0	85.3	109.0	87.3	89.7	104.3	89.1	105.1	77.1	112.0	94.7	98.7	83.5
23	116.3	97.7	115.0	97.5	85.1	108.7	87.3	89.4	103.8	89.0	104.9	76.9	112.0	94.3	98.6	83.7

Real effective exchange rates

Index numbers, 1980-82 average = 100. Each index is the corresponding nominal effective exchange rate adjusted for differential inflation in wholesale prices of nonfood manufactures. Underlying price data are partly estimated. Index revisions reflect revised price information or, less frequently, adoption of new price indices to measure inflation in one or more countries.

	United States	Canada	Japan	Australia	France	Germany	Italy	United Kingdom	Austria	Belgium	Neth-erlands	Spain	Swit-zerland	Den-mark	Norway	Swe-den
1980	89.5	99.6	103.1	93.1	102.2	103.5	103.5	99.2	100.2	107.5	100.0	102.0	98.7	103.7	96.7	101.3
1981	100.7	100.0	104.7	102.8	100.2	97.4	98.7	101.9	99.1	100.3	97.7	99.1	98.8	99.4	101.0	102.1
1982	109.8	100.4	92.3	104.1	97.7	99.1	97.8	98.9	100.7	92.1	102.4	99.0	102.5	96.9	102.4	96.6
1983	112.4	102.9	96.4	99.7	95.8	99.2	99.8	94.5	101.5	91.5	101.6	89.3	105.0	98.5	100.9	91.2
1983																
March	110.6	102.7	98.5	96.3	97.6	101.1	99.7	89.2	103.8	94.0	103.5	90.4	103.0	100.6	99.1	89.0
April	110.4	103.0	96.1	94.6	96.1	100.9	100.1	93.2	102.4	93.0	101.7	90.5	103.9	100.9	100.5	89.4
May	110.3	103.3	96.9	95.4	94.6	100.1	100.2	96.3	101.6	92.7	101.3	90.3	104.1	100.4	100.7	90.0
June	112.6	103.3	95.3	96.6	94.3	99.3	100.0	96.9	101.0	92.3	100.9	89.5	104.0	98.8	101.3	90.9
July	113.3	103.7	95.2	97.2	95.0	98.3	100.1	96.4	101.3	91.8	101.3	87.7	104.7	96.7	100.8	92.5
August	115.2	103.8	93.6	99.3	94.4	98.0	98.9	97.1	100.6	91.2	100.8	87.9	105.7	96.1	100.8	92.9
September	113.9	104.2	94.7	100.7	94.9	98.1	99.3	97.3	100.5	90.5	100.8	88.1	105.5	97.5	102.9	92.1
October	113.2	103.0	97.2	102.2	95.5	98.8	99.5	94.9	101.3	90.0	100.9	87.7	105.7	97.4	102.4	92.2
November	114.3	103.1	97.3	104.0	95.5	97.8	99.6	95.4	100.8	89.4	100.2	88.3	105.7	96.7	102.2	93.1
December	115.4	102.9	98.4	103.6	95.6	97.3	99.7	94.4	100.3	88.8	99.8	88.7	106.5	95.5	101.2	93.9
1984																
January	116.3	102.9	99.2	105.3	95.5	96.8	99.7	94.4	100.1	88.0	99.0	89.8	106.4	94.7	100.6	94.4
February	114.4	102.4	97.8	107.7	96.7	98.0	99.6	94.2	101.1	88.2	99.4	91.2	104.8	95.0	100.0	94.3

Eurocurrency deposit rates

prime banks' bid rates, at or near end of month

	1980	1981	1982	1983						1984	
	Dec	Dec	Dec	Jul	Aug	Sep	Oct	Nov	Dec	Jan	Feb
Eurodollar											
overnight	19.25	12.87	9.25	8.75	9.38	9.25	9.25	9.00	9.50	9.25	9.37
one month	19.12	13.31	9.12	9.81	9.87	9.38	9.44	9.69	9.69	9.50	9.87
three months	17.55	13.75	9.19	10.19	10.25	9.50	9.62	9.75	9.81	9.62	10.12
six months	16.37	14.81	9.50	10.62	10.62	9.69	9.69	9.94	10.06	9.87	10.37
twelve months	14.87	14.75	9.62	10.75	10.94	10.00	9.94	10.31	10.37	10.19	10.81
Euro-Canadian dollar											
one month	17.50	15.37	10.00	9.00	8.87	9.06	8.94	9.25	9.12	9.62	9.62
three months	16.88	15.37	10.00	9.37	9.37	9.13	9.19	9.37	9.50	9.62	9.81
six months	15.37	16.37	10.13	9.87	9.87	9.38	9.37	9.56	9.75	9.87	10.00
twelve months	14.00	16.37	10.25	10.12	10.44	9.75	9.69	9.75	10.00	10.06	10.37
Euro-French franc											
one month	11.12	15.75	23.00	12.12	13.00	12.75	12.25	12.25	12.12	12.12	16.00
three months	11.75	17.00	24.00	13.50	15.00	14.31	12.87	13.19	12.19	13.00	17.25
six months	12.25	18.00	22.00	15.25	16.75	15.81	14.00	14.12	12.31	13.75	16.75
twelve months	12.87	18.25	19.75	16.75	16.88	16.19	14.87	14.69	12.62	14.37	16.13
Euromark											
one month	8.87	10.44	5.87	4.81	5.25	5.56	5.56	6.19	5.25	5.69	5.69
three months	8.87	10.50	5.87	5.06	5.50	5.75	5.81	6.19	5.87	5.87	5.81
six months	8.87	10.56	5.94	5.50	5.94	5.88	5.81	6.19	6.12	6.19	6.94
twelve months	8.93	10.25	6.00	5.94	6.44	6.19	6.12	6.44	6.37	6.37	6.19
Euro-Dutch guilder											
one month	8.87	10.75	5.12	5.44	6.00	5.94	5.75	6.00	5.81	5.87	5.94
three months	9.31	10.75	5.19	5.62	6.25	6.19	6.06	6.19	6.00	5.94	6.00
six months	9.37	10.75	5.38	6.00	6.44	6.25	6.19	6.31	6.25	6.12	6.06
twelve months	9.62	10.75	5.63	6.31	6.75	6.56	6.50	6.62	6.37	6.44	6.44
Euro-Swiss franc											
one month	6.00	8.87	2.81	4.69	4.19	3.69	3.50	4.06	3.37	3.00	3.44
three months	6.00	9.25	3.25	4.75	4.44	4.13	4.12	4.06	3.75	3.44	3.62
six months	5.75	9.25	3.44	4.87	4.81	4.31	4.19	4.19	3.94	3.81	3.87
twelve months	5.50	8.50	3.44	4.81	4.94	4.38	4.31	4.37	3.94	3.94	4.12
Eurosterling											
one month	14.75	15.37	10.56	9.56	9.56	9.63	9.19	9.06	9.12	9.19	9.12
three months	14.75	15.69	10.44	9.81	9.75	9.56	9.25	9.25	9.31	9.37	9.19
six months	14.25	15.69	10.31	10.25	10.12	9.56	9.37	9.44	9.50	9.56	9.31
twelve months	14.00	15.37	10.31	10.50	10.50	9.81	9.69	9.69	9.81	9.87	9.50
Euroyen											
one month	9.12	6.12	6.75	6.44	6.69	6.69	6.12	7.25	6.25	6.12	6.87
three months	9.25	6.12	6.75	6.50	6.62	6.69	6.31	6.75	6.31	6.31	6.56
six months	9.62	6.87	7.10	6.56	6.62	6.69	6.31	6.69	6.38	6.31	6.50
twelve months	9.37	6.87	6.81	6.56	6.75	6.69	6.44	6.69	6.44	6.44	6.62

International bond issues — by currency

new issues with a maturity of three years or more, publicly offered or privately placed in the period
millions of dollars

	1981	1982	1983	1984			Jan-Mar	
				Jan	Feb	Mar	1984	1983
Eurobonds	**31 616**	**51 645**	**48 479**	**6 679**	**8 501**	**4 309**	**19 489**	**11 618**
U.S. dollar	26 830	43 959	38 406	5 771	6 706	3 170	15 647	9 224
Canadian dollar	634	1 201	1 039	112	16	63	191	245
German mark	1 277	2 588	3 817	302	567	77	946	1 205
British pound	501	748	1 947	281	577	514	1 372	14
Japanese yen	368	374	212	—	43	—	43	148
European composite unit	309	1 980	2 019	125	476	338	939	457
Other	1 697	795	1 039	88	116	147	351	325
Foreign bonds	**21 369**	**26 397**	**27 677**	**2 042**	**2 829**	**1 906**	**6 777**	**8 459**
U.S. dollar	7 552	5 946	4 400	200	100	1 079	1 379	1 423
German mark	1 310	2 952	2 671	161	308	77	546	788
Dutch guilder	481	956	1 053	63	157	—	220	374
British pound	746	1 214	811	91	176	29	296	99
Swiss franc	8 285	11 432	14 299	1 236	1 682	649	3 567	4 557
Japanese yen	2 457	3 418	3 772	278	235	67	580	1 118
Other	538	479	671	13	171	5	189	100
Total	**52 985**	**78 042**	**76 156**	**8 721**	**11 330**	**6 215**	**26 266**	**20 077**

International bond issues — by country of borrower

new issues with a maturity of three years or more, publicly offered or privately placed in the period
millions of dollars

	1981	1982	1983	1984			Jan-Mar	
				Jan	Feb	Mar	1984	1983
Industrial countries	**40 861**	**63 062**	**60 281**	**7 337**	**9 752**	**5 850**	**22 939**	**17 121**
Australia	991	2 250	2 394	181	149	135	465	355
Austria	1 557	1 668	1 265	216	233	100	549	490
Belgium	527	211	1 153	—	—	146	146	192
Canada	10 648	11 979	7 411	948	436	485	1 869	2 059
Denmark	695	1 269	1 719	600	273	268	1 141	379
Finland	672	815	866	145	90	163	398	206
France	3 156	8 456	6 461	522	1 404	221	2 147	1 968
Germany	279	1 101	3 095	281	473	117	871	977
Ireland	517	625	959	35	64	—	99	185
Italy	1 108	2 214	1 565	250	82	100	432	230
Japan	6 928	8 397	13 966	1 754	2 557	827	5 138	4 068
Netherlands	630	894	946	106	291	47	444	174
New Zealand	1 107	1 375	560	—	131	—	131	402
Norway	530	832	699	100	25	30	155	186
Portugal	30	206	76	—	21	100	121	46
South Africa	92	374	548	—	96	75	171	182
Spain	444	747	1 470	272	44	204	520	389
Sweden	2 050	2 479	3 812	176	545	905	1 626	1 995
United Kingdom	1 408	1 201	1 398	300	863	287	1 450	176
United States	6 770	14 538	7 486	1 415	1 680	1 377	4 472	1 784
*Other**	722	1 431	2 432	36	295	263	594	678
Developing countries	**4 886**	**5 003**	**2 525**	**466**	**152**	—	**618**	**269**
Latin American countries	**3 658**	**2 480**	**71**	—	—	—	—	**21**
Argentina	195	—	—	—	—	—	—	—
Brazil	60	91	—	—	—	—	—	—
Chile	30	—	—	—	—	—	—	—
Colombia	20	35	—	—	—	—	—	—
Mexico	3 012	1 919	—	—	—	—	—	—
Panama	25	—	21	—	—	—	—	21
Venezuela	291	385	—	—	—	—	—	—
*Other***	—	50	50	—	—	—	—	—
Asian countries	**1 068**	**2 075**	**2 242**	**426**	**152**	—	**578**	**248**
Hong Kong	70	40	50	—	—	—	—	—
India	271	225	60	—	—	—	—	20
Indonesia	97	412	328	—	—	—	—	37
Korea	323	172	556	55	40	—	95	111
Malaysia	—	807	883	350	—	—	350	63
Philippines	99	50	—	—	—	—	—	—
Singapore	30	125	70	—	—	—	—	—
Thailand	93	63	255	21	112	—	133	17
Other	85	181	40	—	—	—	—	—
Middle Eastern and African countries	**160**	**448**	**212**	**40**	—	—	**40**	—
Egypt	—	75	—	40	—	—	40	—
Israel	117	200	135	—	—	—	—	—
United Arab Emirates	—	20	—	—	—	—	—	—
Other	43	153	77	—	—	—	—	—
Centrally planned countries	**75**	**65**	**75**	—	—	—	—	—
China	—	65	50	—	—	—	—	—
Hungary	20	—	—	—	—	—	—	—
*Other****	55	—	25	—	—	—	—	—
International organizations****	**7 163**	**9 912**	**13 410**	**918**	**1 426**	**365**	**2 709**	**2 687**
Total	**52 985**	**78 042**	**76 156**	**8 721**	**11 330**	**6 215**	**26 266**	**20 077**

*Includes multinational organizations. **Includes unallocated. ***Includes COMECON institutions. ****Includes regional development organizations.

International bond yields

average yield of several actively traded, high quality issues with a maturity of 7 to 12 years
at or near end of month

	1980	1981	1982	1983						1984	
	Dec	Dec	Dec	Jul	Aug	Sep	Oct	Nov	Dec	Jan	Feb
United States companies											
Eurodollar	n.a.	n.a.	11.16	11.57	11.50	11.13	11.29	11.41	11.59	11.43	11.77
Euro-German mark	n.a.	n.a.	7.24	7.42	8.04	7.35	7.23	7.23	7.34	7.34	7.26
Swiss franc	n.a.	n.a.	5.61	5.88	5.83	5.78	5.75	5.73	5.73	5.58	5.61
European governments											
Eurodollar	n.a.	n.a.	12.53	12.90	12.67	12.40	12.44	12.52	12.65	12.33	12.58
Euro-German mark	n.a.	n.a.	8.10	8.23	8.19	8.18	8.05	8.07	8.12	8.08	7.63
Swiss franc	n.a.	n.a.	5.36	5.59	5.72	5.61	5.52	5.52	5.59	5.43	5.33

Eurocurrency bank credits — by country of borrower

credits with a maturity of one year or more, publicly announced in period
millions of dollars

	1981	1982	1983	1984			Jan-Mar	
				Jan	Feb	Mar	1984	1983
Industrial countries	**86 022**	**42 571**	**38 528**	**9 693**	**2 643**	**26 969**	**39 305**	**10 064**
Australia	1 680	4 721	2 911	91	45	116	252	735
Belgium	360	1 172	883	—	—	—	—	—
Canada	4 112	3 838	967	640	—	—	640	—
Denmark	1 661	789	1 586	8	10	—	18	1 300
Finland	463	631	283	—	—	—	—	25
France	3 912	5 703	1 700	133	—	—	133	582
Greece	1 039	770	1 085	—	—	350	350	520
Ireland	1 361	401	764	—	—	—	—	41
Italy	6 030	3 757	2 979	365	253	181	799	907
Norway	713	1 769	1 236	—	—	—	—	204
Portugal	1 590	1 388	913	—	179	40	219	—
South Africa	287	1 479	752	—	100	—	100	550
Spain	3 242	1 849	3 041	154	249	195	598	894
Sweden	1 867	649	3 188	—	—	—	—	2 060
United Kingdom	747	1 635	1 328	10	750	—	760	310
United States	54 784	6 516	12 948	8 142	1 050	26 020	35 212	1 183
Yugoslavia	684	719	615	—	—	—	—	600
*Other**	1 490	4 785	1 347	150	7	67	224	153
Developing countries	**45 264**	**41 519**	**32 905**	**7 860**	**1 414**	**911**	**10 185**	**15 561**
Latin American countries	**30 152**	**26 719**	**15 406**	**6 530**	**170**	**—**	**6 700**	**9 841**
Argentina	2 534	1 565	1 750	—	—	—	—	—
Brazil	5 751	5 716	4 475	6 500	—	—	6 500	4 475
Chile	2 204	1 194	1 319	—	—	—	—	—
Colombia	1 030	741	549	—	170	—	170	—
Ecuador	934	815	431	—	—	—	—	—
Mexico	7 530	7 953	5 138	—	—	—	—	5 100
Peru	1 407	1 069	500	—	—	—	—	16
Venezuela	7 559	6 799	237	—	—	—	—	237
*Other***	1 203	867	1 007	30	—	—	30	13
Asian countries	**10 288**	**8 403**	**8 824**	**1 162**	**728**	**732**	**2 622**	**4 005**
India	377	284	809	50	—	—	50	461
Indonesia	725	1 250	1 467	750	15	—	765	1 146
Korea	2 824	2 923	3 250	105	298	632	1 035	870
Malaysia	1 725	1 909	950	—	150	—	150	560
Pakistan	350	455	365	—	—	—	—	73
Philippines	1 257	635	815	—	—	—	—	585
Thailand	692	268	349	—	245	—	245	18
Other	2 338	679	819	257	20	100	377	292
Middle Eastern and African countries	**4 824**	**6 397**	**8 675**	**168**	**516**	**179**	**863**	**1 715**
Algeria	—	26	1 934	—	—	—	—	—
Egypt	63	353	335	—	—	—	—	—
Morocco	774	326	226	20	75	—	95	25
Nigeria	1 802	2 042	1 775	—	—	—	—	33
Turkey	100	277	1 078	—	350	—	350	140
United Arab Emirates	363	93	876	—	—	—	—	690
Other	1 722	3 280	2 451	148	91	179	418	827
Centrally planned countries	**1 791**	**765**	**1 212**	**150**	**429**	**—**	**579**	**218**
East Germany	470	8	392	—	—	—	—	—
Hungary	550	340	683	—	352	—	352	218
Soviet Union	25	374	68	150	—	—	150	—
*Other****	746	43	69	—	77	—	77	—
International organizations***	**302**	**160**	**1 321**	**—**	**—**	**—**	**—**	**21**
Total	**133 379**	**85 015**	**73 964**	**17 703**	**4 486**	**27 880**	**50 089**	**25 864**

*Includes multinational organizations. **Includes unallocated. ***Includes COMECON institutions. ****Includes regional development organizations.

Eurocurrency market size

measured by foreign currency liabilities
at end of period, billions of dollars

	1977	1978	1979	1980	1981	1982		1983		
						Sep	Dec	Mar	Jun	Sep
Gross market size	740	949	1 233	1 524	1 881	2 017	2 057	2 086	2 056	2 133
Nonbanks	135	174	245	327	428	468	474	472	489	515
Official monetary institutions	100	115	145	150	132	105	90	90	84	90
Other banks	505	660	843	1 047	1 301	1 444	1 493	1 524	1 483	1 528
Eurodollars as % of gross	76	74	72	75	78	81	79	80	80	80

Central bank discount rates

at or near end of month

	1980	1981	1982	1983				Current	
	Dec	Dec	Dec	Mar	Jun	Sep	Dec	Mar 29 1984	effective since
United States	13.00	12.00	8.50	8.50	8.50	8.50	8.50	8.50	Dec 15, 82
Canada	17.36	14.66	10.05	9.42	9.42	9.49	9.96	10.78	Mar 29, 84
Austria	6.75	6.75	4.75	3.75	3.75	3.75	3.75	3.75	Mar 18, 83
Belgium	12.00	15.00	11.50	11.00	9.00	9.00	10.00	11.00	Feb 16, 84
Denmark	11.00	11.00	10.00	8.50	7.50	7.50	7.00	7.00	Oct 27, 83
Finland	9.25	9.25	8.50	8.50	8.50	9.50	9.50	9.50	Jul 1, 83
France	9.50	9.50	9.50	9.50	9.50	9.50	9.50	9.50	Aug 31, 77
Germany	7.50	7.50	5.00	4.00	4.00	4.00	4.00	4.00	Mar 18, 73
Ireland	12.75	17.15	14.35	14.35	13.80	12.20	11.50	11.50	Nov 11, 83
Italy	16.50	19.00	18.00	18.00	17.00	17.00	17.00	16.00	Feb 15, 84
Netherlands	8.00	9.00	5.00	3.50	4.50	5.00	5.00	5.00	Sep 9, 83
Norway	9.00	9.00	9.00	9.00	8.00	8.00	8.00	8.00	Jun 6, 83
Portugal	18.00	18.00	19.00	23.00	23.00	25.00	25.00	25.00	Aug 10, 83
Spain	8.00	8.00	8.00	8.00	8.00	8.00	8.00	8.00	Jul 26, 77
Sweden	12.00	11.00	10.00	9.00	8.50	8.50	8.50	8.50	Apr 8, 83
Switzerland	3.00	6.00	4.50	4.00	4.00	4.00	4.00	4.00	Mar 18, 83
United Kingdom	14.00	14.37	10.00	10.50	9.56	9.50	9.00	9.00	Oct 4, 83
Japan	7.25	5.50	5.50	5.50	5.50	5.50	5.00	5.00	Oct 22, 83
New Zealand	14.00	13.00	13.00	13.00	13.00	13.00	13.00	13.00	Jul, 81
South Africa	7.00	13.50	13.50	13.50	13.50	13.50	13.50	13.50	Dec 12, 81
Argentina	87.01	98.50	128.54	145.29	161.87	183.75	183.75	134.13	Feb 1, 84
Korea	15.01	10.50	5.00	5.00	5.00	5.00	5.00	5.00	Mar 29, 82
Philippines	4.00	4.00	4.00	4.00	4.00	4.00	4.00	4.00	May 19, 78
Singapore	10.50	9.50	7.00	7.00	7.00	7.00	7.00	7.00	Feb 19, 82
Thailand	13.50	14.50	12.50	11.50	11.50	11.50	13.00	13.00	Dec 9, 83
Venezuela	13.00	14.00	13.00	13.00	11.00	11.00	11.00	11.00	May 18, 83

Day-to-day money rates

monthly averages

	1980	1981	1982	1983						1984	
	Dec	Dec	Dec	Jul	Aug	Sep	Oct	Nov	Dec	Jan	Feb
United States	18.90	12.37	8.95	9.37	9.56	9.45	9.48	9.34	9.47	9.56	9.59
Canada	15.61	14.53	10.63	9.31	9.35	9.25	9.35	9.43	8.78	9.60	9.63
Austria	11.50	7.50	6.00	5.00	5.00	5.00	5.62	5.62	5.75	5.87	5.87
Belgium	9.68	12.78	9.43	7.49	7.61	6.38	6.89	8.58	8.65	8.03	7.57
Finland	12.50	11.30	11.50	15.00	15.00	16.67	16.95	16.70	16.70	17.50	17.50
France	10.87	15.46	12.88	12.40	12.54	12.56	12.35	12.37	12.27	12.39	12.30
Germany	9.13	10.65	6.07	5.04	5.07	5.43	5.53	5.59	5.60	5.61	5.55
Ireland	13.31	16.88	14.54	13.75	12.50	12.62	11.00	12.25	12.19	12.12	11.25
Italy	17.50	20.63	19.00	17.75	17.88	17.69	17.75	17.79	17.88	17.91	17.67
Netherlands	8.37	10.67	5.31	5.29	5.77	5.68	5.82	5.70	5.84	5.77	6.12
Norway	11.00	18.60	11.00	12.00	12.70	12.30	13.50	13.00	13.00	12.80	11.45
Spain	16.74	18.73	20.30	21.05	23.33	19.85	20.27	18.56	16.41	10.16	12.14
Sweden	11.41	13.82	8.63	11.00	10.15	11.30	12.00	11.97	11.48	11.36	10.90
Switzerland	5.75	3.38	1.25	3.00	2.00	2.00	1.75	1.62	1.88	1.00	1.62
United Kingdom	13.00	9.13	6.70	6.60	6.31	7.30	7.81	7.06	7.77	7.31	7.12
Australia	9.51	12.84	11.04	9.84	10.13	9.80	9.03	9.31	4.56	7.09	9.05
Japan	9.49	6.70	6.92	6.39	6.48	6.53	6.43	5.93	6.47	6.05	6.04
South Africa	5.60	12.34	12.90	12.29	13.62	13.43	13.66	14.24	15.63	16.17	16.19
Argentina	70.84	84.93	155.32	210.04	106.40	175.30	178.30	178.30	178.30	138.61	128.53
Brazil	62.71	103.74	150.42	224.98	207.06	193.91	192.62	193.91	184.69	224.27	295.48
Hong Kong	14.05	10.75	9.13	7.00	6.81	13.25	18.00	10.00	13.90	7.25	3.31
Korea	14.82	14.40	13.84	12.70	12.70	12.80	12.80	12.90	11.40	11.30	10.50
Philippines	15.70	14.70	16.12	13.59	15.56	16.54	24.23	18.96	31.18	n.a.	n.a.
Singapore	10.23	3.96	11.45	8.08	6.33	6.51	7.02	7.23	7.05	6.92	6.83

Treasury bill rates

bond equivalent yields, at or near end of month

	1980	1981	1982	1983						1984	
	Dec	Dec	Dec	Jul	Aug	Sep	Oct	Nov	Dec	Jan	Feb
United States	14.87	11.90	8.15	9.50	9.52	9.05	8.92	9.05	9.28	9.20	9.48
Canada	17.01	14.41	9.80	9.24	9.32	9.24	9.24	9.38	9.71	9.73	9.82
Belgium	12.75	16.00	12.25	9.25	9.25	9.25	9.50	10.85	10.85	10.85	12.25
Ireland	12.84	17.35	14.70	13.09	13.01	12.12	11.96	11.66	11.63	11.80	12.16
Italy	16.87	21.36	19.11	17.35	17.24	17.18	17.08	17.05	16.95	15.74	15.89
Netherlands	8.00	9.75	5.62	5.38	6.00	5.87	5.62	5.62	5.63	5.75	6.12
Spain	n.a.	n.a.	15.28	14.51	14.64	14.60	14.52	14.53	14.46	13.61	13.66
Sweden	n.a.	n.a.	12.90	11.60	11.55	12.20	12.10	12.10	11.75	11.10	11.15
United Kingdom	13.45	15.31	9.90	9.40	9.57	9.21	8.89	9.08	9.08	9.08	9.08
Australia	12.17	13.27	9.39	10.59	10.96	10.34	9.38	9.32	8.54	9.43	10.35
Japan	5.93	5.42	5.42	5.42	5.42	5.42	4.91	4.91	4.91	4.91	4.91
New Zealand	11.25	11.25	11.25	7.80	7.80	7.80	7.80	7.80	7.80	7.80	7.80
South Africa	6.31	14.55	14.62	14.46	16.19	14.91	15.66	17.47	18.43	18.55	18.57
Brazil	65.87	92.62	115.40	174.00	197.30	163.92	179.15	179.15	179.15	179.15	179.15
Mexico	27.73	33.33	57.44	61.10	57.89	56.17	54.50	53.85	n.a.	n.a.	n.a.
Philippines	12.74	13.40	14.53	14.03	14.48	14.71	15.04	15.56	15.98	n.a.	n.a.
Singapore	6.77	3.03	2.74	2.59	2.58	2.65	2.63	2.62	2.59	2.67	2.65

Representative money market rates

bond-equivalent yields on major short-term (mostly 3-4 month) money market instruments other than Treasury bills, at or near end of month

	1980	1981	1982	1983						1984	
	Dec	Dec	Dec	Jul	Aug	Sep	Oct	Nov	Dec	Jan	Feb
United States	17.62	12.78	8.81	9.57	9.52	9.36	9.26	9.31	9.75	9.36	9.68
Canada	17.50	15.25	9.95	9.40	9.50	9.40	9.40	9.60	9.87	9.85	9.95
Belgium	13.10	16.00	12.35	9.25	9.25	9.25	9.50	10.75	11.00	11.00	12.50
France	11.56	15.25	12.75	12.13	12.25	12.50	12.19	12.31	12.19	12.25	12.54
Germany	10.20	10.50	6.20	5.50	5.85	5.80	6.15	6.25	6.30	6.10	5.85
Ireland	13.62	18.50	15.75	13.87	13.38	12.69	12.53	12.37	12.19	12.25	12.56
Italy	17.37	21.00	19.00	17.50	17.60	17.50	17.63	17.88	17.88	17.88	17.00
Netherlands	9.37	11.00	5.25	5.69	5.31	6.25	6.12	6.31	6.00	5.94	6.00
Portugal	11.00	13.80	15.04	17.00	20.24	22.30	23.00	24.17	24.11	24.06	23.79
Spain	17.40	15.52	16.55	22.48	24.04	22.06	22.19	20.29	18.48	17.39	18.30
Switzerland	7.50	10.12	3.67	5.00	4.75	4.25	4.25	4.25	3.87	3.62	3.75
United Kingdom	14.75	15.69	10.50	10.06	9.75	9.56	9.31	9.25	9.31	9.37	9.21
Australia	13.00	16.00	10.65	12.10	12.20	11.15	11.00	10.60	9.50	11.00	13.00
Japan	9.80	6.30	6.80	6.59	6.61	6.62	6.30	6.42	6.42	6.30	6.40
New Zealand	14.25	16.05	16.75	12.75	10.25	10.00	10.75	12.00	12.10	13.85	15.00
South Africa	7.12	15.47	15.26	14.94	16.61	16.45	16.94	18.19	19.12	19.07	19.01
Chile	26.79	34.54	71.44	25.34	23.87	25.34	25.34	25.34	22.42	19.56	14.03
Hong Kong	17.69	14.18	10.13	9.87	8.94	12.75	16.88	11.50	12.84	11.37	7.87
Indonesia	12.54	14.48	18.50	14.50	15.00	16.50	15.00	15.00	19.50	19.00	20.50
Korea	16.35	15.69	8.00	8.00	8.00	8.00	8.00	8.00	8.00	8.00	8.00
Malaysia	9.41	9.50	8.50	7.85	8.40	8.10	8.20	8.65	9.80	9.47	8.51
Philippines	15.01	17.61	15.89	15.96	15.62	16.49	18.26	17.34	15.60	n.a.	n.a.
Singapore	14.12	7.81	8.69	7.87	7.37	7.37	7.50	7.62	8.44	7.75	7.75
Taiwan	14.49	10.94	9.94	8.98	9.27	8.37	7.82	7.26	7.65	9.22	9.42
Thailand	16.55	14.29	12.25	12.00	12.75	14.00	14.25	14.50	16.00	16.50	17.00

Commercial bank deposit rates

at or near end of month

	1980	1981	1982	1983						1984	
	Dec	Dec	Dec	Jul	Aug	Sep	Oct	Nov	Dec	Jan	Feb
United States	16.25	12.62	8.25	9.65	9.65	9.20	9.30	9.30	9.70	9.40	9.77
Canada	17.00	15.20	9.85	9.35	9.45	9.35	9.35	9.50	9.82	9.80	9.90
Austria	11.25	9.63	6.25	5.31	5.56	6.06	6.31	6.37	6.50	6.50	6.25
Belgium	12.63	15.50	12.25	9.12	9.25	9.50	9.38	11.25	11.25	10.87	12.37
Denmark	10.00	10.00	9.00	6.50	6.50	6.50	6.00	6.00	6.00	6.00	6.00
Finland	5.00	5.00	4.25	5.25	5.25	5.25	5.25	5.25	5.25	5.25	5.25
France	11.25	9.16	8.24	8.24	7.30	7.80	7.70	7.70	7.66	7.72	n.a.
Germany	8.00	9.50	6.00	4.90	4.90	5.63	5.60	5.80	5.90	5.65	5.40
Ireland	13.62	18.38	15.25	13.50	13.13	12.25	12.50	12.25	11.75	11.87	12.37
Italy	13.25	13.25	13.25	13.25	13.25	13.25	13.25	13.25	13.25	13.25	13.25
Netherlands	9.50	11.00	5.37	5.63	5.25	6.12	6.06	6.19	6.13	5.94	6.00
Norway	11.00	12.75	13.50	12.50	12.50	12.50	12.50	12.50	12.75	13.00	12.50
Portugal	12.00	14.00	15.00	19.50	21.50	21.50	21.50	21.50	21.50	21.50	21.50
Spain	4.50	11.78	12 53	12.28	12.28	12.24	12.08	12.50	12.62	n.a.	n.a.
Sweden	13.20	12.65	12.15	11.30	12.20	12.05	12.20	12.30	11.70	11.00	11.10
Switzerland	7.50	8.75	3.00	4.00	3.75	3.75	3.50	3.50	3.50	3.25	3.25
United Kingdom	14.87	15.69	10.31	10.06	9.78	9.50	9.25	9.22	9.31	9.37	9.25
Australia	12.71	15.65	10.20	12.05	11.88	10.56	10.96	10.35	10.40	11 25	12.20
Japan	9.00	6.50	7.00	6.80	6.83	6.88	6.45	6.60	6.50	6.52	6.63
New Zealand	13.50	15.50	16.50	10.00	9.00	9.00	9.50	10.75	11.50	13.75	10.00
South Africa	7.87	14.75	15.25	14.95	16.62	17.00	17.00	18.43	20.13	19.45	18.88
Argentina	72.00	86.76	103.42	127.75	139.92	176.41	176.41	176.41	176.41	139.91	121.66
Brazil	54.00	110.05	21.00	23.00	24.50	25.00	26.00	24.00	23.00	26.00	25.00
Chile	39.45	36 87	57.72	24.31	24.75	25.19	25.19	25.19	22.28	19.74	12.95
Hong Kong	13.00	12.50	7.50	8.50	8.50	12.00	10.00	9.00	9.00	7.00	5.50
Korea	14.82	14.40	7.60	7.60	7.60	7.60	7.60	7.60	7.60	6 00	6.00
Malaysia	8.60	10.00	8.40	6.80	6.80	7.15	7.15	7.60	7.75	7.75	7.75
Mexico	26.15	31.82	52.54	59.25	57.33	56.38	55.20	54.84	54.70	54.50	n.a.
Philippines	14.00	14.00	14.00	14.00	14.00	14.00	14.00	14.00	14.00	14.00	14.00
Singapore	13.19	7.50	8.25	7.44	6.88	6.81	7.07	7.19	7.44	7.13	7.19
Taiwan	10.25	10.75	7.50	7.00	7.00	7.00	7.00	7.00	7.00	7.00	7.00
Thailand	9.00	10.00	10.00	10.00	10.00	10.00	10.00	10.00	10.00	10.00	10.00
Venezuela	16.00	14.75	15.50	13.50	13.00	12.50	12.00	12.00	12.00	11.50	11.50

Domestic government bond yields

long-term issues, at or near end of month

	1980	1981	1982	1983						1984	
	Dec	Dec	Dec	Jul	Aug	Sep	Oct	Nov	Dec	Jan	Feb
United States	11.46	14.33	10.61	11.95	11.77	11.65	11.85	11.89	12.00	11.72	12.13
Canada	12.69	15.27	11.69	12.03	12.34	11.76	11.73	11.80	12.02	11.92	12.40
Austria	9 62	10 37	8.81	8.18	8.31	8.32	8.16	8.06	8.02	7.96	n.a.
Belgium	13.04	13.99	12 66	11.42	11.46	11.39	11.32	11.75	11.89	11.97	12.35
Denmark	19.98	20.91	20.14	15.56	14.92	14.19	13.95	14.22	12.96	13.39	n.a.
Finland	10.42	10.98	10.64	10.58	11.20	10.97	11.19	11.16	11.16	11 17	10.62
France	14.31	16.44	15.40	14.04	13.96	14.03	14.15	14.12	13.96	13.76	13.78
Germany	9.19	9.71	7.90	8.27	8.55	8.43	8.30	8.34	8.38	8.33	8.13
Ireland	15.63	18.28	14.54	13.81	13.60	13.72	13.82	13.72	14.25	13.94	14.16
Italy	16.23	21.39	19.70	18.42	18.11	17.82	17.65	17.78	17.69	17.09	16.33
Netherlands	10.48	11.28	8.16	9.08	9.03	8.80	8.53	8.57	8.58	8.57	8.56
Norway	10.44	12.37	13 32	12.50	12.50	12.50	12.50	12.50	12.50	12.50	12.25
Portugal	17.19	17.39	16.63	19.30	21.57	21.97	22.05	22.80	n.a.	n.a.	n.a.
Spain	16.15	16.20	15.92	17.60	18.31	18.76	19.47	19.50	18.71	18.33	n.a.
Sweden	12.61	12.80	13.01	11.85	11.24	12.20	12.24	13.05	12.30	11.70	11.50
Switzerland	4.63	5.40	4.22	4.76	4.73	4.71	4.61	4.62	4.52	4 31	4.38
United Kingdom	13.05	15.02	10.62	10.71	10.65	10.15	10.13	9.93	9.94	9.97	10.04
Australia	13.00	15.00	13.00	15.00	14.60	14.40	13.70	13.40	13.65	13.70	14.05
Japan	9.04	8.32	7.76	7.87	7.80	7.58	7.51	7.39	7.19	7.20	7.06
New Zealand	12.99	12.55	12.84	14.02	10.41	10.13	10.58	10.61	10.53	n.a.	n.a.
South Africa	11.81	13.33	11.31	13.29	13.40	13.14	13.29	13.60	13.70	14.18	13.52
Philippines	13.41	13.41	13.41	13.41	13.41	13.41	13.41	13.41	13.41	13.41	13.41
Venezuela	7.39	12.50	15.00	15.00	15.00	14.00	14.00	14.00	13.50	13.00	13.00

Commercial bank lending rates to prime borrowers

at or near end of month

	1980	1981	1982	1983						1984	
	Dec	Dec	Dec	Jul	Aug	Sep	Oct	Nov	Dec	Jan	Feb
United States	21.50	15.75	11.50	10.50	11.00	11.00	11.00	11.00	11.00	11.00	11.00
Canada	18.25	16.50	12.50	11.00	11.00	11.00	11.00	11.00	11.00	11.00	11.00
Austria	12.50	13.50	11.75	9.25	9.25	9.25	9.25	9.25	9.25	9.25	9.25
Belgium	15.75	18.00	15.50	12.50	12.50	12.50	12.50	13.25	13.75	13 75	14.75
Denmark	13.75	15.00	14.00	10.50	10.50	10.50	10.50	10.00	10.00	10.00	10.00
Finland	9.83	9.84	8.95	10.07	10.10	10.16	10.14	10.15	10.18	10.30	n.a.
France	12.25	14.00	12.25	12.25	12.25	12.25	12.25	12.25	12.25	12.25	12.25
Germany	11.50	13.00	8.75	7.75	7.75	7.75	7.75	7.75	7.75	7.75	7.75
Ireland	14.50	17.25	16.50	15.00	15.00	13.75	13.75	13.75	13.75	13.75	13.75
Italy	20.50	22.50	20.75	18.75	18.75	18.75	18.75	18.75	18.75	18.50	18.50
Netherlands	10.75	12.00	6.25	6.25	6.75	7.00	6.75	6.50	7.00	6.75	6.75
Norway	12.50	13.75	14.50	13.38	13.13	13.50	13.25	13.75	13.50	13.63	13.75
Portugal	18.75	20.50	23.50	27.50	30.00	30.00	30.00	30.00	30.00	30.00	30.00
Spain	18.50	17.04	19.00	23.47	25.19	24.09	23.70	22.87	20.85	20.01	n.a.
Sweden	14.00	15.00	15.00	13.50	13.50	13.50	13.50	13.50	13.50	13.50	13.50
Switzerland	5.75	8.00	6.00	6.00	6.00	6.00	6.00	6.00	6.00	6.00	6.00
United Kingdom	14.00	14.50	10.00	9.50	9.50	9.50	9.00	9.00	9.00	9.00	9.00
Australia	13.50	15.75	15.00	14.50	14.50	14.00	13.25	13.25	12.75	11.50	13.00
Japan	8.16	6.95	6.28	6.25	6.24	6.23	6.23	6.08	5.89	5.89	5.70
New Zealand	13.00	13.00	13.00	13.00	11.00	11.00	11.00	11.00	11.00	11.00	11.00
South Africa	9.50	17.00	18.00	16.00	18.00	18.00	18.00	19.00	20.00	20.00	20.00
Argentina	77.00	92.60	109.50	240.00	152.08	188.58	188.58	188.58	188.58	152.08	133.83
Brazil	120.10	152.40	23.81	24.00	24.00	24.00	24.00	24.00	24.00	24.00	24.00
Chile	49.55	61.43	85.19	43.14	37.50	39.83	40.60	40.40	35.11	31.43	22.75
Hong Kong	17.00	16.00	10.50	11.50	11.50	16.00	15.00	13.50	13.50	11.50	10.00
Indonesia	21.00	19.25	22.00	22.00	19.00	19.50	19.50	19.50	19.75	20.00	21.25
Korea	19.50	16.50	10.00	10.00	10.00	10.00	10.00	10.00	10.00	10.00	10.00
Malaysia	8.50	12.00	12.50	10.75	11.00	11.00	11.00	11.00	11.00	11.00	11.00
Mexico	24.25	31.81	46.12	58.73	58.23	57.78	57.14	56.82	56.44	55.95	55.16
Philippines	16.00	18.00	18.00	18.00	18.00	18.00	18.00	18.00	18.00	18.00	18.00
Singapore	13.60	11.83	9.33	9.00	9.00	8.95	8.93	8.93	8.98	9.05	9.03
Taiwan	16.20	15.25	10.75	10.25	10.25	10.25	10.25	10.25	10.25	10.25	10.25
Thailand	16.50	17.00	16.00	16.00	15.50	15.50	15.50	16.00	16.00	16.00	16.50
Venezuela	15.00	15.50	17.00	16.50	16.25	16.00	16.00	16.00	16.00	16.00	14.50

Domestic corporate bond yields

long-term issues, at or near end of month

	1980	1981	1982	1983						1984	
	Dec	Dec	Dec	Jul	Aug	Sep	Oct	Nov	Dec	Jan	Feb
United States	13.00	15.50	11.75	12.75	12.50	12.25	12.63	12.38	12.63	12.38	12.88
Canada	13.53	16.18	12.74	13.03	13.13	12.54	12.57	12.58	12.89	12.78	13.27
France	15.23	17.33	15.91	14.76	14.48	14.36	14.62	14.30	14.06	13.96	n.a.
Germany	9.50	10.50	8.20	8.00	8.10	8.30	8.30	8.30	8.30	8.30	8.00
Netherlands	10.71	11.03	7.80	8.75	8.79	8.68	8.39	8.53	8.51	8.44	8.39
Norway	11.24	13.36	14.13	13.25	12.25	13.25	13.25	13.25	13.25	13.25	13.00
Spain	14.82	14.76	17.10	18.00	19.59	20.05	20.37	20.03	19.84	20.19	20.69
Sweden	11.95	12.94	13.37	12.85	12.77	12.99	12.40	12.51	12.21	12.15	n.a.
Switzerland	n.a.	n.a.	4.87	4.88	5.08	5.07	4.94	4.94	4.94	4.93	n.a.
United Kingdom	14.21	16.65	12.34	12.34	12.27	11.89	11.84	11.51	11.57	11.52	11.61
Australia	14.25	16 50	15.00	15.75	15.50	15.00	15.00	15.00	13.50	14.00	14.50
Japan	8.60	7.70	7.55	7.34	7.32	7.30	7.29	7.27	7.09	7.05	7.04
Korea	28.20	26.90	15.90	13.90	13.90	14.20	14.10	14.20	14.20	14.30	14 00
Venezuela	16.15	17.00	18.00	18.00	18.00	18.00	18.00	18.00	18.00	18.00	17.50

Key to data in tables

I. International markets

An *international bond* issue is one sold outside the country of the borrower. It may be either a Euro-bond issue or a foreign bond issue.

A *Euro-bond* issue is one underwritten by an international syndicate and sold principally in countries other than the country of the currency in which the issue is denominated.

A *foreign bond* issue is one underwritten by a syndicate composed of members from one country, sold principally in that country, and denominated in the currency of that country.

Data on *new international bond issue volume* include all publicly announced issues with an original maturity of three years or more, whether publicly or privately placed, but exclude those where the investor is a central bank, monetary authority, or government.

A *Euro-currency bank credit* is a loan in a currency which is not native to the country in which the bank office making the loan is located.

Data on *new Euro-currency bank credit volume* include all publicly announced loans with an original maturity of one year or more. A loan is included in the period in which the lending banks make a commitment covering the amount and terms of the loan to the borrower.

The *country of the borrower* is the residence of the borrowing entity, except where the entity is a financing vehicle, in which case the residence of the parent company and or guarantor is used.

Data on *Eurocurrency market size* are based on foreign currency liabilities of banks in major European countries, the Bahamas, Bahrain, Canada, Cayman Islands, Hong Kong, Japan, Netherlands Antilles, Panama, Singapore, and the United States (international banking facilities only).

II. Domestic markets

Day-to-day money rates

Argentina — 7-day interbank money regulated by the Central Bank.

Austria — day-to-day interbank rate.

Australia — approximate effective interest rate in the authorized short-term money market.

Belgium — interbank call money.

Brazil — interbank overnight money.

Canada — chartered banks' day-to-day loans.

Finland — Bank of Finland call money.

France — interbank call money against private paper.

Germany — interbank call money.

Hong Kong — interbank 24-hour call rate.

Ireland — interbank call money.

Italy — interbank 48 hour call money.

Japan — Tokyo interbank call money, unconditional lenders rate.

Korea — call money.

Netherlands — open-market call money.

Norway — day-to-day interbank rate.

Philippines — interbank call money.

Singapore — interbank overnight money.

South Africa — National Finance Corporation call money.

Spain — day-to-day interbank rate.

Sweden — interbank call money.

Switzerland — call money.

United Kingdom — call money.

United States — effective Federal funds rate.

Treasury bill rates

Australia — new issues of 13-week Treasury notes.

Belgium — 3-month Treasury certificates.

Brazil — 3-month Treasury bills.

Canada — 3-month Treasury bills at tender.

Ireland — 3-month Central Bank Exchequer bills.

Italy — 6-month Treasury bills.

Japan — 60- to 62-day noninterest-bearing discount government bills.

Mexico — 3-month Federal Treasury bills.

Netherlands — 3-month Treasury bills.

New Zealand — 3-month Treasury bills.

Philippines — 91-day Treasury bills at tender.

Singapore — 91-day Treasury bills at tender.

South Africa — 3-month Treasury bills at tender.

Spain — Bank of Spain 3-month certificates of deposit used for monetary correction until March 1982. New series as of April 1982, 6-month Treasury bills.

Sweden — new issues of 3-month Treasury bills until June 1982. New series as of July 1982, 6-month Treasury discount notes, market rate.

United Kingdom — 91-day Treasury bills at tender.

United States — 3-month Treasury bills.

Representative money-market rates

Australia — 3-month prime finance company paper.

Belgium — 4-month Fonds des Rentes certificates.

Canada — 3-month prime finance company paper.

Chile — 60-day Central Bank promissory notes (PDBC).

France — 3-month interbank money against private paper.

Germany — 3-month interbank deposits.

Hong Kong — 3-month interbank deposits.

Indonesia — 1-month interbank deposits.

Ireland — 3-month interbank deposits.

Italy — 3-month interbank deposits.

Japan — 3-month repurchase agreements.

Korea — 3-month financial bill.

Malaysia — 3-month interbank deposits.

Netherlands — 3-month interbank deposits.

New Zealand — 90-day commercial bills.

Philippines — 90-day promissory notes.

Portugal — average of 30- to 90-day interbank deposits.

Singapore — 3-month bank acceptances.

South Africa — 90-day bank acceptances.

Spain — 1-month interbank deposits.

Switzerland — 3-month interbank deposits.

Taiwan — interbank call money.

Thailand — interbank call money.

United Kingdom — 3-month interbank deposits.

United States — 3-month prime industrial paper.

Commercial bank deposit rates

Argentina — nominal 30-day time deposits. Average of bank rates published by the Central Bank.

Austria — 3-month time deposits.

Australia — 3-month certificates of deposit.

Belgium — special maximum rate for 3-month time deposits in large amounts.

Brazil — 6-month certificates of deposit with prefixed yields until July 1982. New series as of August 1982, 6-month certificates of deposit reported as a spread above monetary correction.

Canada — 3-month time deposits.

Chile — 30-day time deposits.

Denmark — time deposits of 3-months' notice.

Finland — time deposits of six-month notice.

France — 3-month time deposits of FF. 1,000,000.

Germany — 3-month time deposits in large amounts.

Hong Kong — 3-month certificates of deposit. Rate set by the Hong Kong Association of Banks.

Ireland — 3-month time deposits.

Italy — 3-month time deposits of Lit. 100 million or more.

Japan — 90-day negotiable certificates of deposit issued by the Tokyo office of Morgan Guaranty Trust Company.

Korea — 3-month time deposits.

Malaysia — 3-month time deposits.

Mexico — 3-month certificates of deposit issued by financieras to corporations for amounts over Ps. 1 million. Higher rates available to individuals.

Netherlands — 3-month time deposits in large amounts.

New Zealand — 6-month transferable certificates of deposit.

Norway — 3-month special term deposits.

Philippines — 3-month time deposits.

Portugal — 90- to 180-day time deposits.

Singapore — 3-month certificates of deposit.

South Africa — negotiable certificates of deposit.

Spain — maximum legal rate for 3-month deposits until May 1981. New series as of June 1981, deposits over 6-months and less than 1-year for Pts. 1 million or more reported by the Bank of Spain.

Key to data in tables — continued

Sweden — 3-month certificates of deposit.

Switzerland — 3-month time deposits.

Taiwan — 3-month time deposits.

Thailand — 3-month time deposits.

United Kingdom — 3-month time deposits.

United States — 3-month negotiable certificates of deposit issued by Morgan Guaranty Trust Company.

Venezuela — 6-month negotiable certificates of deposits for domestic depositors only.

Domestic government bond yields

Austria — Austrian National Bank average yield on all outstanding government bonds.

Australia — 20-year government bonds.

Belgium — Belgian National Bank average yield on government bonds maturing in more than five years.

Canada — Bank of Canada average yield on all direct government bonds due or callable in 10 years or more.

Denmark — 12% serial bonds maturing 2001 until April 1983. New series as of May 1983, 10% serial bonds maturing 2004.

Finland — rate of interest at issue on central government bonds intended for public subscription, weighted by sales of bonds in the latter half of each month.

France — Institut National de la Statistique et des Etudes Economiques (INSEE) yield on public and semi-public sector bonds.

Germany — Frankfurter Allgemeine Zeitung (FAZ) 7% public authority bond average until September 1978. New series as of October 1978, FAZ 10-year public authority bond average.

Ireland — 15-year government bonds.

Italy — average yield on fixed-interest government bonds, not including irredeemable bonds, weighted by the amounts in circulation, for maturities of 9-years or more.

Japan — secondary market yield for the 6.1% due 1988 national government bond.

Netherlands — Central Bureau of Statistics (CBS) average yield on three latest government bonds.

New Zealand — average yield on government bonds maturing after 10 years.

Norway — 5% government bond of 1996 until December 1982. New series as of January 1983, average yield of long-term government bonds.

Philippines — Central Bank 5-year Certificate of Indebtedness, regular issue.

Portugal — yield of 4% Centenary Loan of 1940.

South Africa — 25-year government bonds until August 1983. New series, as of September 1983, 20-year Republic of South Africa bonds.

Spain — weighted average of yields of several central government issues with original maturity of less than five years.

Sweden — 15-year government bonds until October 1983. New series as of November 1983, 5-year government bond yield index, market rate.

Switzerland — Swiss Confederation bond average.

United Kingdom — F.T. (Financial Times) Actuaries 25-year government stock.

United States — Morgan Guaranty 20-year U.S. Government Bond Index.

Venezuela — Banco Central average yield on public-sector bond issues.

Commercial bank lending rates to prime borrowers

Argentina — average rate on 30-day loans.

Austria — overdraft rate for prime borrowers, including commission.

Australia — approximate overdraft rate for prime borrowers.

Belgium — prime overdraft rate.

Brazil — prefixed rate applied to working capital loans until July 1982; monetary-corrected free rate applied to working capital loans from August 1982 to July 1983. New series as of August 1983, maximum legal rate reported as a spread above monetary correction.

Canada — prime rate.

Chile — average prime rate of six major commercial banks.

Denmark — approximate rate for loans and advances to prime borrowers.

Finland — average rates on total commercial bank lending.

France — base lending rate, excluding a commission of .05% per month on highest debit balance during the month. A spread above base rate is often added.

Germany — approximate effective overdraft rate for prime borrowers.

Hong Kong — prime rate.

Indonesia — prime rate for domestic affiliates of foreign companies.

Ireland — AA corporate borrowing rate.

Italy — unsecured overdraft rate for prime borrowers.

Japan — average contracted interest rate for short-term loans of city banks. In addition, compensating balances may be required.

Korea — prime rate.

Malaysia — Bank of Commerce Berhad base lending rate.

Mexico — base rate or average cost of money for banks determined monthly by the Banco de Mexico S.A.

Netherlands — overdraft rate for prime borrowers, including commission.

New Zealand — overdraft rate for prime borrowers.

Norway — overdraft rate, including a commission of .25% per quarter on the total line of credit until January 1983. New series as of February 1983, special rate of first class, large borrowers.

Philippines — maximum legal rate, for unsecured loans exclusive of service fee.

Portugal — maximum rate for 90- to 180-day loans.

Singapore — most common overdraft rate, major banks.

South Africa — unsecured overdraft rate for prime borrowers.

Spain — preferential rate for 1-month loans calculated by the Bank of Spain.

Sweden — overdraft rate for prime industrial borrowers, commission not included.

Switzerland — unsecured overdraft rate for prime borrowers, excluding commission of .25% per quarter on average or highest outstanding debit balance in quarter.

Taiwan — maximum rate for 3- to 12-month secured loans. Rate is an indication only and may vary from actual bank lending rate which is subject to volatile interbank rates.

Thailand — prime rate.

United Kingdom — clearing bank base lending rate. A spread above base rate is often added.

United States — prime rate of Morgan Guaranty Trust Company.

Venezuela — representative rate for domestic prime borrowers only.

Domestic corporate bond yields

Australia — new issue yields for AA corporate bonds having a maturity of 5- to 7-years.

Canada — McLeod, Young, Weir Co. Ltd., weighted long-term bond yield index for AA corporates.

France — INSEE tax-adjusted average yield on outstanding private corporate bonds.

Germany — Bundesbank average yield on industrial bonds.

Japan — secondary market yield for NTT bond maturing March 1987.

Korea — average of yields on 3-year corporate bonds guaranteed by local banks.

Netherlands — CBS average yield on three 6% to 6.5% corporate bonds until December 1981. New series as of January 1982, yield of domestic long-term bonds issued by major banks.

Norway — 5.75% Dalen Portland-Cement bond of 1969-1984 until December 1982. New series as of January 1983 average yield of long-term industrial bonds.

Spain — average yield for a selected group of electricity companies.

Sweden — Central Satistical Bureau average yield on industrial bonds.

Switzerland — average yield on outstanding bonds of four leading Swiss companies. Mixture changed as of January 1982.

United Kingdom — F.T. (Financial Times) Actuaries 20-year debentures and loans until February 1981. New series as of March 1981, F.T. Actuaries 25-year debentures and loans.

United States — Salomon Brothers index of new issue yields for Aa industrial bonds with five-year call protection.

Venezuela — average of yields on 15-year bond issues of Electricidad de Caracas.

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World Financial Markets

Morgan Guaranty Trust Company of New York

May 1984

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Mexico: progress and prospects

Mexico has made notable economic and financial progress since it shocked the international financial community in August 1982 by declaring a temporary moratorium on external debt payments. The emergency program arranged late that year averted a breakdown of international financial markets and set the pattern for dealing with the debt-servicing difficulties of other LDCs. Mexico's economic adjustment policies and their implementation under President Miguel de la Madrid are perceived as having been successful. Indeed, Mexican performance has been cited as a showcase for programs supported by the International Monetary Fund.

Foreign commercial banks, encouraged by Mexico's achievements in 1983, completed in April a new loan of $3.8 billion to meet 1984's commercial borrowing needs. In recognition of improved performance, the spreads on this loan are lower, and the maturity and grace period longer, than those of last year's $5 billion loan. Mexico's active role in arranging a $500 million short-term financing package for Argentina with the participation of Brazil, Colombia, Venezuela, and foreign commercial banks affirms its commitment to seeking constructive ways to cope with the worst economic crisis to hit Latin America in five decades.

Mexico's experience provides an instructive case study in macroeconomic adjustment. This article reviews the country's progress to date, analyzes issues facing the authorities in 1984, and explores longer-term challenges that need to be overcome in order for Mexico to achieve adequate and stable economic growth.

Origins of the 1982 crisis

Mexico's balance of payments crisis was the culmination of several years of flawed economic policies supported by unsustainable foreign borrowing. The crisis was precipitated by a sharp deterioration of the current account and massive capital flight. Starting in 1981 the Mexican government failed to respond in a timely and constructive manner to three adverse external events: lower world oil prices, higher international interest rates, and deep recession in the United States — the market that absorbs more than 60% of Mexico's exports of goods and services.

The seeds of the problem were planted in 1978, when the govern-

ment embarked on very expansionary policies. By full-speed exploitation of newly found, abundant petroleum reserves, oil production and exports were the key ingredients in a high-growth strategy that was spearheaded by heavy public-sector spending. Crude petroleum production rose from 1.2 million barrels per day in 1978 to 2.8 million barrels per day in 1982. The volume of oil exports expanded by about 40% per annum during this period, while their value rose nearly ninefold, from less than $2 billion in 1978 to almost $16 billion in 1982. By that year, roughly three-quarters of merchandise export earnings derived from petroleum, and oil-related receipts provided nearly half of all public-sector revenues. Unrestrained public-sector spending, which far outstripped oil revenues, became the driving force in the economy. Public-sector expenditures rose from 32% of GDP in 1978 to 48% in 1982, and increased the fiscal deficit from 6.7% of GDP in 1978 to 18% in 1982.

As a result of this expansionary economic policy, real GDP growth averaged a record 8.4% per annum between 1978 and 1981. For the first time in recent memory employment expanded faster (5.2% per annum) than the labor force (nearly 4%). The inevitable result, however, was strong pressure on prices and the balance of payments. Inflation was kept just below 30% per annum only by increasing subsidies, tightening price controls, and an artificially strong peso, which encouraged a virtual tripling in merchandise imports and caused non-oil exports to stagnate. The outcome was a growing deficit on current account. This exceeded $16½ billion at an annual rate in the second half of 1981, up from a deficit of only about $3 billion in 1978.

The authorities chose not to abandon their all-out growth policies even when the external environment turned sharply adverse in mid-1981. Instead they resorted to even higher levels of foreign borrowing. Confidence in the government's economic policies eventually disappeared as such corrective measures as import restrictions and peso devaluations proved ineffectual in reversing basic trends. Capital flight, already significant for several years, increased sharply with the fear of further devaluations and exchange controls. Capital outflows exceeded $9 billion in 1982, for a cumulative total of more than $25 billion for 1978-82. In the end, external borrowing sufficient to finance these current and capital account gaps could not be procured, and by August 1982 the country's foreign exchange resources were depleted. Between end-1978 and mid-1982, Mexico's external debt ballooned by over $50 billion to more than $85 billion, or about 280% of the country's exports of goods and services. Moreover, the maturity of this debt had steadily shortened as lender confidence waned, so that by the time the temporary moratorium was declared close to one-third of the total debt was short term.

The 1983 adjustment program

The cornerstone of the stabilization strategy adopted by President de la Madrid's government has been an adjustment program developed within the context of a three-year, $3.9 billion Extended IMF Facility. This program enabled Mexico to negotiate with its commercial bank creditors a new-money facility of $5 billion disbursed during 1983 and the rescheduling of nearly $23 billion of public-sector, short- and medium-term external debt falling due through the end of 1984. In addition, through a scheme known as FICORCA, provision was made for the restructuring of nearly $12 billion of

Table 1

Main quarterly targets of the 1983 economic adjustment program

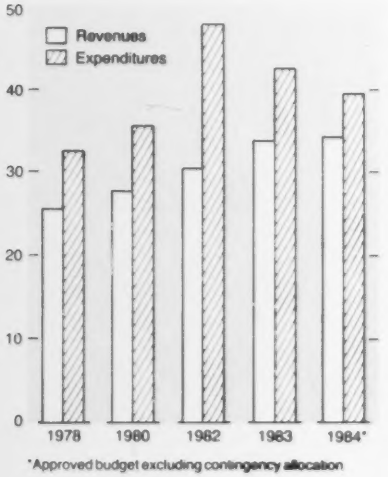
end-of-period data

	Q1	Q2	Q3	Q4
Central bank claims on the nonfinancial public sector (billions of pesos)				
Target ceiling	2.4	2.6	2.7	3.0
Actual	2.3	2.4	2.4	3.0
Net domestic assets of the central bank (billions of pesos)				
Target ceiling	0.6	0.6	0.6	0.7
Actual	0.4	0.3	0.0	0.5
Public-sector external debt ($ billions)				
Target ceiling	68.0	69.3	70.6	71.8
Actual	67.8	68.6	67.6	71.5
Net international reserves of the central bank ($ billions)				
Target	—0.5	0.0	0.5	1.5
Actual	0.8	1.4	3.1	5.0

Chart 1

Public-sector revenues and expenditures

as percent of GDP



*Approved budget excluding contingency allocation

private short- and medium-term debt, about two-thirds of the total.

The objective of the stabilization program was to reestablish internal and external equilibrium through a combination of restrictive fiscal, wage, and monetary policies, and modifications of other key prices in the economy, principally the exchange rate and interest rates. Quarterly performance criteria to monitor progress were agreed with the IMF (see Table 1). Fiscal policy aimed to cut the public-sector deficit to 8.5% of GDP through expenditure reductions, revenue increases in public-sector entities, higher levies on domestic oil consumption, and an increased value added tax.

The fiscal objective was met. Public-sector expenditures fell over 5% relative to GDP, while receipts increased by nearly 4% of GDP (see Chart 1). Although interest payments increased over 40% in real terms, and accounted for nearly one-third of total public-sector expenditure, there were cutbacks in real terms in practically all other major spending categories, most notably in subsidies. These were brought down 40% in real terms through major hikes in the controlled prices of petroleum products, electricity, and foodstuffs. The government's more realistic pricing policy, including the partial elimination of widespread price controls, improved resource allocation by restraining consumption of key goods such as oil products and electricity. Besides the cutback in current spending, public-sector capital outlays were slashed 30% in real terms.

Reduction in real wages was critical to the improvement of public finances. The public-sector wage bill dropped 20% in real terms, the equivalent of nearly two percentage points of GDP. The government was able to elicit the cooperation of the labor union movement to keep nominal wage increases below inflation. In return, price increases on basic foods were trimmed to avoid too drastic a reduction in the consumption standards of a large part of the population. Even so, minimum wages in real terms fell over 16% in 1983, for a cumulative drop of 26% since 1981 (see Chart 2). This set the tone for private- and public-sector wage adjustments, and helped to minimize the drop in employment throughout the economy.

Monetary policy aimed at increasing the proportion of domestic savings channeled through the banking system and at limiting credit expansion with the help of a smaller public-sector deficit. Interest rates on most financial instruments were raised early in 1983 in line with expected levels of inflation. They remained negative in real terms during the early part of the year as inflation accelerated, but turned positive in the second half as it abated. Savings deposited in banks rose 66%, but still lagged behind inflation. They thus declined in real terms, although to a lesser extent than in the previous year. The 52% credit expansion to the private sector was held down by the drop in economic activity, and contributed to considerable liquidity in the banking system. Net financing to the public sector registered only a 43% growth (compared with 139% a year earlier) and was instrumental in cutting by nearly half the expansion of the monetary base. In all, the IMF targets for overall credit expansion by the central bank were met.

The introduction of exchange controls and the major devaluations of 1982 resulted in a dual exchange rate system. It consists of a lower, controlled rate applicable to merchandise exports, debt servicing, and most imports, and a higher so-called free rate for most services and other payments. On a real effective basis, the controlled exchange rate depreciated by nearly 37% be-

Chart 2

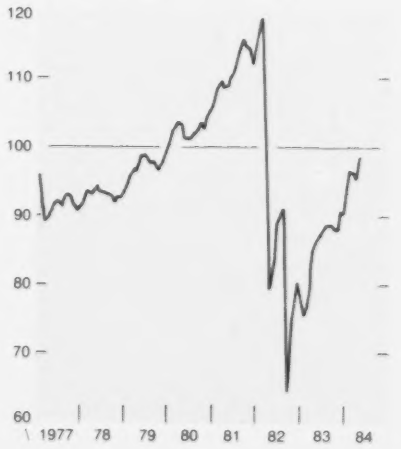
Average real wages

annual percent change

Chart 3

Real effective peso exchange rate

index, 1980-82 = 100



tween January and December 1982 (see Chart 3). Since then, it has been devalued daily by 13 Mexican cents per dollar — not enough, however, to compensate for the inflation differential between Mexico and its main trading partners. As a result, the real effective peso exchange rate appreciated nearly 14% in 1983, giving up more than half the 1982 gain in international price competitiveness. The "free" rate, originally set about 55% higher than the controlled rate, was held fixed until late September 1983 when the central bank began to devalue it by the same daily amount as the controlled rate. As a result, the differential narrowed to 12%.

This combination of fiscal, wage, monetary, and exchange rate policies contributed to an unprecedented real GDP decline of 4.7% in 1983, considerably worse than the assumption of zero growth made at the beginning of the program. However, toward the end of last year the rate of decline of industrial output slowed significantly (see Chart 4). Although inflation had been originally assumed to fall from almost 100% in 1982 to 55% by year-end 1983, it closed the year at 80.8% (see Chart 5). The pace of inflation, however, slowed during the second half of the year to an annualized 64%. The difference in actual versus officially forecasted output and inflation performance can be attributed to an initial underestimation of the gravity of the fiscal imbalance and the magnitude of the exchange rate and price adjustments that were required to achieve the public-sector deficit reduction and to bring stability to the foreign exchange market.

The most striking results of Mexico's adjustment program showed in the balance of payments. Last year the current account balance swung into a surplus of $5.5 billion, far better than the $3.4 billion deficit originally expected (see Table 2). This stemmed from a large drop in merchandise imports, to only $7.7 billion in 1983, far below the $15.2 billion initially projected and a full 68% down from the peak level registered in 1981.

Merchandise exports barely held their own last year. Crude oil export revenues declined 5% to $14.8 billion. Volume rose nearly 3%, but the average realized price fell 8%. Among non-oil exports, only manufactured exports recorded vigorous expansion (22%), led by steel and metal products. Actual non-oil exports almost certainly increased more than indicated by the official figures which do not reflect under-invoicing, stimulated by the dual exchange rate regime and the existence of an even more attractive rate in the uncontrolled market for pesos outside Mexico.

The current account turnaround, together with the restructuring of public short- and medium-term debt payments and the $5 billion commercial bank loan arranged in 1983, permitted a $3.1 billion increase of gross foreign exchange reserves, which reached a level of $4.9 billion at year-end. In contrast to the turnaround in the current account, there were no net reflows of private capital. Indeed, there were net outflows amounting to almost $5 billion, partly through debt payments by private firms via the free peso market, and the nonremittance of earnings on assets held abroad by Mexican residents. The full-year 1983 figure may well have included spillover of capital flight spurred by the 1982 crisis, for example, the repatriation of investments held by nonresidents in so-called Mex-dollar deposits.

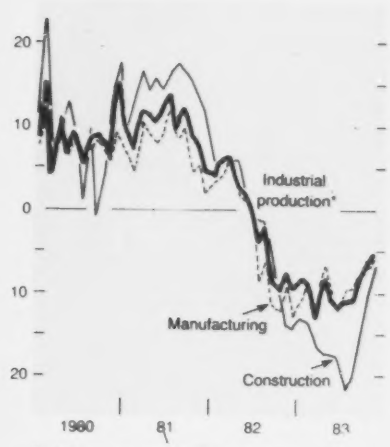
Policy challenges in 1984

Mexico's remarkable progress last year entailed considerable short-

Chart 4

Industrial production

monthly data,
percent change from previous year

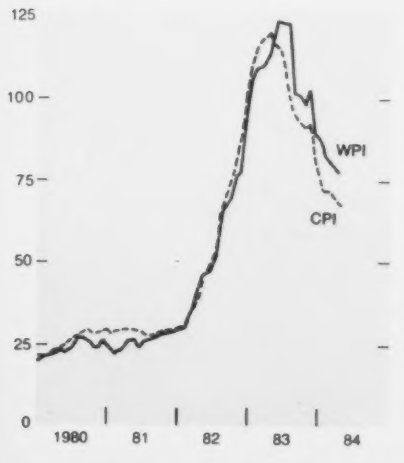


*Includes mining, manufacturing, construction and electric power

Chart 5

Consumer and wholesale prices

monthly data,
percent change from previous year



term costs in terms of employment and incomes. The country's political leadership and institutions were and will continue to be tested. The enormous problems they face in the areas of demand management and resource allocation cannot be quickly corrected. The task is not made easy in view of the internal pressures for early relief from high inflation and deep recession, not to mention political opposition to the government party. Perseverance with corrective policies is essential, however, if the full long-term benefits of the adjustment program are to be reaped, and confidence fully restored, both at home and abroad.

This year, through steady, conservative management of aggregate demand, the stabilization program aims for an upturn in domestic economic activity — yielding at least 1% real GDP growth and a recovery of private-sector investment — along with a reduction of inflation to 40% on a year-end basis. The achievement of both objectives is to be supported by a significant expansion of imports, by as much as 75% above 1983 levels, even though this is anticipated to wipe out the current account surplus.

Progress on the fiscal front is to be maintained, as evidenced by a target deficit for the public sector of 5.5% of GDP, down from 8.7% in 1983. The bulk of this improvement is to come from continued containment of expenditures, principally operational outlays. Further price hikes for public goods and services, either above or in line with inflation, will increase revenues in real terms.

Although the cutbacks required to meet this year's fiscal objectives are considerably smaller than in 1983, for several reasons they will be just as difficult to achieve. First, interest payments on both domestic and external debt now account for nearly a third of total spending. Second, the investment budget already has been pruned, so that the scope for further cuts is much reduced. Third, following last year's major real wage reductions, labor unions can be expected to resist additional losses, thus making difficult any significant lowering in the government's real wage bill. Fourth, the sense of urgency prevalent a year ago has diminished and administrators throughout the public sector have become both more identified with their respective programs and more aware of pressures for economic recovery. Notwithstanding these obstacles, the authorities remain committed to slashing the fiscal deficit in line with the agreed target.

Wage policy under the program calls for salary adjustments to be kept in line with expected inflation. An improvement in real wages is not contemplated at this time, although living standards of the lowest-paid workers are to be protected by concentrating the remaining subsidies on basic consumer goods. A critical test for wage policy will come shortly when the midyear wage adjustments are decided. Actual inflation, 80% at an annual rate in the first four months of 1984, is running considerably ahead of the 40% inflation objective embodied in this year's program. Failure to compensate for most of the gap between actual and anticipated inflation would, of course, imply yet another fall in real wages — a trend likely to be resisted by the Mexican Workers Confederation, until now a key cooperative force in Mexico's stabilization effort. Nominal wage increases higher than originally budgeted, however, would set back efforts to contain public-sector expenditures.

Monetary policy in 1984 aims to support the inflation and growth objectives of the program. The targeted 30% increase of net credit to the public sector is to be kept below the expected inflation rate. It is to be funded through noninflationary

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Table 2

Balance of payments

$ billions

	1982	*1983*	*1984**
Merchandise exports	21.2	21.4	22.1
Merchandise imports	—14.4	—7.7	—11.9
Trade balance	6.8	13.7	10.2
Interest payments	—11.3	—9.9	—11.7
Other services and transfers	—0.4	1.7	2.6
Current account balance	—4.9	5.5	1.0
Net capital flows	0.2	—2.3	2.0
Change in gross reserves	—3.2	3.1	3.0

*Estimated.

sources. This credit expansion is consistent with the projected reduction in the fiscal deficit, and would finance about three-fifths of the fiscal deficit. External financing would cover the remainder. Credit to the private sector is envisaged to grow in real terms by the equivalent of nearly 1% of GDP to support the expected private-sector recovery.

Interest rates are to be kept positive in real terms for most financial savings instruments, as they were during a good part of 1983. Reforms are to be undertaken in the structure of reserve requirements, in the cost of preferential credit, and in the pricing of banking services. These reforms should lessen distortions in credit allocation and reduce the large spread between current deposit and lending rates.

The most problematic of the monetary objectives will be the maintenance of positive real interest rates, which are indispensable to stimulate domestic savings and discourage capital flight. Indeed, there is concern among officials that the current level of interest rates, though below the rate of inflation in the first four months, may be too high to permit the recovery of private-sector investment spending. Any attempts to bring down interest rates ahead of actual inflation, however, would jeopardize a much-needed rise in real terms of domestic savings held in the banking system. Besides, it is not clear that reductions in the cost, or substantial increases in the availability, of bank credit would appreciably change the prospects for an upturn in private investment. At the moment, a very cautious attitude prevails in the private sector, related more to uncertainties about the government's view of the role for private enterprise in Mexico's development than to the impact of high interest rates.

It is noteworthy that the government obtained from the IMF some leeway for the allowable fiscal deficit in the 1984 economic program, in the event that private-sector spending fails to recover as quickly as desired. A spending reserve equivalent to 1% of GDP may be used in the second half of the year if economic activity does not recover and provided that noninflationary financing is available. There might well be strong pressure to activate this fiscal reserve in order to finance employment-creating public investment projects.

Consistent with a modest recovery of economic activity and the need to ease bottlenecks and shortages that are contributing to inflation, this year's IMF program envisions a liberalization of imports. Merchandise imports, which had been cut by two-thirds from their 1981 peak level, are expected to rise from under $8 billion in 1983 to $13½ billion in 1984 through a relaxation of import duties, quotas, and permits imposed at the height of the payments crisis. This will narrow the trade surplus from $13.7 billion to about $9 billion, since crude oil export volumes and prices are assumed to remain virtually unchanged and an expected 15% rise in non-oil exports will yield only an additional $1 billion in earnings. Accordingly, officials project the current account balance to swing from a $5½ billion surplus to a $1 billion deficit. Financing from official and private sources, including $3.8 billion from commercial banks, is to cover this modest current account deficit, along with repayments of principal (mainly to official agencies) not subject to rescheduling, and also to permit a $2 billion increase in international reserves.

Critical to Mexico's balance of payments performance this year is the evolution of exchange rate policy. The present pace of minidevaluations, equivalent to about 33% over a 12-month period, would maintain

external competitiveness at the end-1983 level only if domestic inflation does not exceed 40% in 1984. But in the first quarter, domestic prices rose 16.2%, as measured by the wholesale price index (excluding food), while the peso depreciated by 8.4% against the dollar, and by 7.4% on a trade-weighted basis. Thus, on a real effective basis, the peso appreciated by nearly 6% considerably eroding Mexican competitiveness. Clearly, a continuation of this trend could seriously impede the achievement of external payments objectives, despite the strong U.S. economic expansion that otherwise augurs well for Mexican exports. Continued real appreciation also may deter import substitution in Mexico and further delay reflows of private capital from abroad. While real appreciation of the peso alleviates inflationary pressures by constraining increases in the prices of tradable goods in the near term, experience shows that the anti-inflationary benefits are only temporary and are outweighed by the costs of lost international competitiveness.

Another factor that will have a bearing on this year's current account result is the trend in overseas interest rates. Official projections assume that the effective interest rate on external debt will average about one percentage point higher than 1983's 11%. This assumption will hold if market rates of interest do not rise higher than present levels. Given that much of Mexico's foreign debt is on a floating-rate basis, every one-percentage-point variation from the posited interest rate translates into a $700 million change in interest payments over the course of a year.

An additional uncertainty revolves around the 1984 level of imports. There can be little doubt that imports will recover strongly this year. Data on U.S. exports to Mexico during the first quarter — up 33% over the first quarter of last year — confirm that a healthy upturn is on the way. This is understandable considering how far inventories of imported goods were depleted during 1982-83 and how tightly imports were restricted through quantitative controls. What is difficult to judge is how quickly import demand will react to the liberalization of these controls, the real appreciation of the peso, and the degree of private-sector recovery. In fact, it is more likely that Mexican imports this year may increase to no more than $12 billion, a 56% rise, rather than by 75% to $13½ billion. In this event, the current account may continue to show a surplus (see Table 2).

Challenges beyond 1984

Notwithstanding the progress made so far in Mexico's stabilization program, further improvements of aggregate demand and exchange rate policies are needed to lay a firm foundation for longer-term economic growth. Beyond this, additional policy efforts will be required to bring about a change in the pattern of that growth. Future growth ought to be more labor-intensive and more reliant on domestic savings than that achieved during the oil boom, or indeed in the postwar period. Increased labor absorption is required to provide gainful employment opportunities — not only to those presently unemployed or partially employed (estimated at 12% and 50% of the labor force, respectively), but also to the projected 800,000 new entrants into the job market every year. Oil revenues and foreign savings cannot be relied upon to the extent they were in the recent past.

Oil export revenues will not provide stimulus for the economy as they did during 1978-82, when their annual growth rate surpassed 70%. With proven oil reserves of 48 billion

barrels at end-1983 (sixth largest in the world), the country could technically boost its output in the future. However, given the weak world demand for oil and an ample supply outlook, substantial growth of Mexican oil production could undermine an orderly international market. The volume of exports can therefore be expected to expand roughly in line with world demand, or at slightly more than 1% per annum. World oil prices are likely to remain fairly flat in nominal terms through 1985 and may subsequently rise no more than expected world inflation. This implies that crude oil export revenues may grow from $15.2 billion in 1984 to about $21.5 billion in 1990, an average of only 6% per annum.

Projected financing availabilities during the rest of the 1980s imply that Mexico may see an outward flow of domestic savings equivalent on average to 3% of GDP. This contrasts sharply with the experience during the 1978-81 period. The accelerated pace of external borrowing in those years resulted in an inflow of net financial transfers of a similar magnitude. The corresponding shift in the direction of net resource flows is an integral part of the longer-term adjustment process. Given the limited prospective growth in oil export revenues, it is essential in order to lower the external debt burden and to gradually reestablish creditworthiness. A sound way to ease balance of payments constraints is thus to improve the domestic savings effort, increase the capacity of future investment to generate new jobs, and expand non-oil export earnings.

As noted earlier, in years to come the public-sector investment program should emphasize employment-generating rather than capital-intensive activities. The 1984 budget has made a start in this direction by reducing investment allocations for large energy and industrial projects in favor of more labor-absorptive activities such as roads, agriculture, and urban infrastructure. Further progress in improving the composition of the investment program should be possible through better project analysis and investment planning. The technical and financial assistance of organizations such as the World Bank and the Inter-American Development Bank could make a useful contribution to this effort. The Mexican authorities also can enhance the overall employment-generating capacity of the economy by eliminating remaining factor-price distortions, such as interest rate levels and fiscal incentives that lower the relative price of capital and thereby promote capital-intensive investment. Similarly, payroll taxes and other indirect labor costs work against a capital/labor mix that reflects the country's resource endowment. Unless the capability of the economy to generate employment improves significantly, unemployment will worsen and illegal emigration to the United States will persist, exacerbating friction between the two countries.

A more dynamic and competitive private sector would be another vehicle for improving resource allocation and raising productivity. Over time, the direct participation of the state in production activities has become widespread. Public-sector enterprises number nearly 400, span almost 70 industrial branches, and account for over one-third of industrial output or about 12% of GDP. Bureaucratic and political considerations have exerted a strong influence in their decision making and have led to very low productivity and poor operating results in many. Moreover, state-imposed price controls, although significantly reduced from their peak in 1982, continue to play a deciding role in determining profit margins in key sectors such as steel, where private participation is important.

A resurgence of private investment is necessary to achieve economic recovery and sustained growth, particularly given the tight investment budget of the public sector. Private-sector confidence in government policies, however, is critical to this end. Currently, a "wait and see" attitude permeates the private sector, in part reflecting weak domestic demand and unutilized capacity in many manufacturing subsectors. The private sector also appears uncertain of the role it will be allowed to play within the context of the government's economic strategy. At issue is the basic government philosophy that the state is the nation's main economic agent. Recalling the previous government's elimination of the Mex-dollar deposits, imposition of exchange controls, and nationalization of private banks, the concern about continued statism is not conducive to stimulating private-sector initiative. This concern has been reinforced by the regulatory measures recently introduced for the automotive and pharmaceutical industries. Government directives now stipulate specific deadlines for the size and type of automobiles to be produced, and set local-content requirements. Extensive price controls are envisioned in pharmaceuticals, together with preferential treatment for locally owned companies.

Important decisions regarding the role of the private sector still await the long-delayed sectoral development plans. These indicative plans could provide an excellent opportunity to turn back the ubiquitous role of the state and stimulate private investment. A good start was made with the announced plan to dispose of a large portion of company shares held by the nationalized banks. More substantive progress might come from curtailing the number of state enterprises engaged in commercial and production activities and from further reducing the number of products subject to price controls. These measures should be combined with continued liberalization of imports to promote the competitiveness of private firms, which has often lagged because of a protected domestic market. Unless reversed, continued statism would jeopardize the potentially dynamic contribution to economic growth that only a revitalized private sector can provide. If the private sector is reduced to the role of passive adjunct to the state, self-sustained growth coupled with price and balance of payments stability are only too likely to prove elusive.

Enhanced private-sector competitiveness also is essential if non-oil merchandise exports and services are to play a growing role in generating foreign exchange revenues. Considerable potential exists for the expansion of these exports given the size and proximity of the U.S. market, the modest market share of many Mexican products in world markets, and the low wage rates prevailing in Mexico. Non-oil export expansion depends on the maintenance of international cost advantages through a sound exchange rate policy, which, coupled with lower import protection, would foster an outward orientation in locally established firms. A more accommodating attitude toward imports on the part of industrialized countries would provide much-needed positive incentive for Mexican export development by local producers.

A resurgence of foreign investment would be another instrument for stimulating Mexico's growth and productivity. Foreign investment can make significant contributions in such areas as employment creation, technology transfer, efficient import substitution, and export growth. The basis for foreign investment participation in Mexico's economy may well be different in the future than it was in the oil boom

Table 3

Net borrowing requirements and external debt

annual averages, $ billions

	1983-84	1985-87	1988-90
Trade balance	12.0	7.6	6.0
Current account balance	3.3	—1.9	—4.1
Net borrowing requirements	4.0	3.4	5.6
Net resource transfers	—10.5	—8.7	—7.4
Growth of external debt (% change)	4.5	3.5	5.0
Debt to exports ratio at end of period (%)	303	265	226

period. During that period, the rapidly expanding domestic market provided the primary motivation for investment decisions. Moreover, macroeconomic policies encouraged the use of imported inputs in production processes, discouraged exports, and stimulated external borrowing as opposed to equity capital participation. For the foreseeable future, by contrast, potential foreign investors will be facing more modest growth in the domestic market and more limited access to foreign exchange.

Accordingly, now more than before, the government's foreign investment policy needs to provide stable and clear regulations and procedures. The government is aware of this but has opted not to change the existing foreign investment law out of concern for the political controversy it might generate within the government party. Recent guidelines providing for a more flexible and selective application of existing regulations were disappointing insofar as foreign investors had sought more concrete and permanent assurances in the form of new legislation. Under present arrangements, government administrators will continue to have considerable discretionary powers in deciding the merits of individual proposals on a case-by-case basis. Moreover, the criteria of flexibility and selectivity could be subject to different interpretations over time. Such a system is open to arbitrariness and procedural delays, and may not be conducive to the desired strong recovery in foreign investment.

A more central role for the private sector in the country's development plans also would promote a return flow of capital transferred abroad in recent years. There are two important conditions for drawing at least a portion of this capital back on a permanent basis. One is the consistent application of interest rate and exchange rate policies that reward potential investors with attractive and stable returns on domestic financial instruments relative to lower-risk alternatives abroad. The second is the creation of a local investment climate that provides profitable investment opportunities for equity capital on a long-term basis. At present, interest and exchange rate policies are based on an expected inflation rate which is considerably below actual inflation. Such policies not only deter a return of capital, but could contribute to renewed outflows.

Summary

In the immediate period ahead, Mexico needs to consolidate the commendable progress made up to now in redressing the most glaring problems inherited from the oil boom period. Public-sector finances and the balance of payments are presently on a much more solid footing. Despite improved aggregate demand policies, however, inflation remains above the expected level because of the pressures stemming from essential price increases combined with much-reduced import levels. The latter source of pressure can be expected to abate over the course of the year as imports climb back from the unusually low level of 1983. Concern with inflation should not deter the authorities from continuing to pursue steadfastly the policies initiated late in 1982. In particular, interest rate and exchange rate policies need to be brought more in line with actual as opposed to expected inflation in order to avoid retrogression on the domestic savings and external fronts.

Over the longer term, appropriate macroeconomic policies, combined with other measures aimed at enhancing the competitiveness and employment-generation capacity of the economy, would permit Mexico

to regain satisfactory rates of growth and to keep current account deficits within manageable bounds. Principally through sustained trade surpluses, these deficits could be held substantially below those registered during the last two decades relative to exports of goods and services. Smaller current account deficits together with a recovery of foreign investment would permit a narrowing of the country's net borrowing requirements in line with the expected limited availability of external financing over the coming years. This should be attainable under a reasonably stable world economic environment. An annual average growth rate of the foreign debt of about 4%-5% per annum (see Table 3) is feasible and consistent with a per capita economic growth rate of about 3% per annum. This rate of debt accumulation is well below that expected for exports and somewhat less than the likely pace of global inflation. Thus, Mexico ought to be able to trim gradually the level of its debt in real terms and regain creditworthiness. Over the course of the decade, the debt to exports ratio could be brought down steadily from a level of over 300% in 1983 to about 225% in 1990. In the next three years, continued good performance would facilitate rescheduling of maturing bank debt and could allow Mexico's annual new money requirements from foreign banks to remain relatively small — $1-$2 billion — thus establishing the basis for a resumption of normal access to international credit markets.

Statistical appendix

for key to data in tables see April 1984 issue.

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Information herein is from sources considered to be reliable but is furnished without responsibility on the part of Morgan Guaranty Trust Company.

Nominal effective exchange rates

Index numbers, 1980-82 average = 100. Each index shows a currency's trade-weighted appreciation or depreciation measured against 15 other major currencies, using averages of daily noon spot exchange rates in New York and bilateral trade weights based on 1980 trade in manufactures. Annual figures are calendar year averages.

	United States	Canada	Japan	Australia	France	Germany	Italy	United Kingdom	Austria	Belgium	Netherlands	Spain	Switzerland	Denmark	Norway	Sweden
Pre-June 1970 parities	114.6	114.4	69.0	116.4	111.1	66.2	226.2	147.5	80.6	91.1	82.1	143.2	51.3	113.0	92.3	119.6
Smithsonian central rates	103.1	121.9	77.2	116.7	109.8	68.9	220.9	146.7	80.6	92.3	82.9	142.7	53.2	110.8	90.9	117.6
1980	90.7	100.4	95.5	96.0	106.5	100.0	108.4	99.8	99.4	105.9	100.2	106.5	95.4	105.1	98.2	103.9
1981	99.5	100.2	105.8	104.0	100.4	97.2	98.8	102.1	98.9	101.8	97.1	99.4	98.3	99.2	100.1	103.3
1982	109.8	99.4	98.6	100.1	93.1	102.8	92.8	98.1	101.7	92.3	102.7	94.1	106.3	95.7	101.7	92.8
1983	114.2	100.8	107.8	92.0	87.3	107.6	90.3	91.6	103.6	90.0	105.0	78.4	111.5	96.4	99.4	82.2
1983																
May	112.2	100.6	107.9	88.2	86.8	108.5	90.8	92.9	104.0	90.8	104.8	79.5	110.6	97.5	99.3	81.7
June	114.3	100.8	106.6	89.4	86.4	107.6	90..	93.6	103.4	90.2	104.6	78.3	110.6	96.2	99.5	82.2
July	115.1	101.0	106.9	89.8	86.2	107.2	90.6	93.4	103.5	89.7	104.5	76.8	111.7	95.4	99.9	82.6
August	117.0	101.2	106.2	91.5	85.6	106.5	89.6	94.0	103.1	89.2	104.1	77.0	112.3	94.5	100.3	82.8
September	116.7	101.3	107.1	92.2	85.6	106.9	88.9	93.8	103.3	88.8	104.2	76.7	112.4	94.9	100.9	82.6
October	114.8	101.0	110.7	93.5	85.4	108.0	88.6	92.2	103.8	88.7	105.0	76.0	113.2	95.2	100.8	82.3
November	116.5	100.9	110.7	94.8	85.1	107.1	88.3	92.8	103.2	88.4	104.4	75.9	112.8	94.6	100.9	82.7
December	118.0	100.4	112.1	94.2	84.7	106.8	88.0	91.8	102.8	88.2	104.1	75.8	113.8	94.0	99.5	83.1
1984																
January	119.1	100.5	113.3	95.5	84.1	106.5	87.6	91.5	102.6	87.7	103.7	76.3	113.8	93.6	99.2	83.4
February	117.3	100.2	111.9	97.3	84.7	108.0	87.0	91.4	103.5	88.3	104.3	77.1	112.2	94.0	99.0	82.9
March	115.4	98.0	114.7	97.2	85.3	109.1	87.2	89.8	104.2	89.0	105.0	77.2	111.7	94.6	98.7	83.5
April	116.7	97.5	115.7	95.1	85.2	108.6	87.3	88.9	104.1	89.0	104.8	78.1	111.3	94.0	98.9	83.7
March 30	115.5	97.4	115.3	96.1	85.5	109.2	87.1	89.1	104.2	89.1	105.2	77.5	111.5	94.5	98.6	83.6
April 6	116.0	97.5	115.3	95.9	85.4	109.0	87.4	88.7	104.4	89.0	105.0	77.7	111.5	94.2	98.9	83.8
13	116.0	97.4	115.9	94.2	85.3	108.9	87.7	88.9	104.1	89.0	105.0	77.8	111.3	94.2	98.8	83.5
20	116.7	97.4	115.9	94.9	85.1	108.5	87.4	88.7	104.3	89.1	104.8	78.3	111.2	94.1	99.2	83.7
27	117.4	97.6	116.0	95.2	85.0	108.2	87.1	88.9	104.2	88.7	104.7	78.4	111.2	93.8	99.1	83.7
May 4	118.3	97.0	115.9	96.3	84.8	107.9	86.8	89.4	103.8	88.7	104.3	78.3	110.9	93.6	99.2	83.7
11	119.7	96.8	115.5	95.6	84.4	107.4	86.8	89.5	103.5	88.7	104.3	78.3	110.8	93.4	99.2	83.6

Real effective exchange rates

Index numbers, 1980-82 average = 100. Each index is the corresponding nominal effective exchange rate adjusted for differential inflation in wholesale prices of nonfood manufactures. Underlying price data are partly estimated. Index revisions reflect revised price information or, less frequently, adoption of new price indices to measure inflation in one or more countries.

	United States	Canada	Japan	Australia	France	Germany	Italy	United Kingdom	Austria	Belgium	Netherlands	Spain	Switzerland	Denmark	Norway	Sweden
1980	89.5	99.6	103.1	93.0	102.2	103.5	103.5	99.3	100.2	107.5	100.0	102.0	98.7	103.7	96.7	101.3
1981	100.7	100.0	104.7	102.8	100.2	97.4	98.7	102.1	99.1	100.3	97.7	99.0	98.8	99.4	101.0	102.1
1982	109.8	100.4	92.3	104.2	97.7	99.1	97.8	98.6	100.7	92.2	102.4	99.0	102.5	97.0	102.4	96.6
1983	112.6	103.0	96.5	99.9	95.9	99.3	100.0	93.0	101.6	91.7	101.8	89.5	105.2	98.6	101.1	91.4
1983																
May	110.5	103.3	97.0	95.7	94.8	100.3	100.3	94.6	101.7	92.9	101.5	90.5	104.3	100.6	100.9	90.2
June	112.7	103.4	95.4	96.8	94.4	99.4	100.2	95.2	101.1	92.5	101.1	89.6	104.2	99.0	101.5	91.1
July	113.4	103.7	95.3	97.4	95.2	98.5	100.3	94.9	101.3	91.9	101.4	87.8	104.9	96.9	101.0	92.7
August	115.4	103.8	93.7	99.6	94.5	98.1	99.0	95.4	100.6	91.6	101.0	88.0	105.9	96.2	101.0	93.1
September	114.1	104.4	94.8	100.9	95.0	98.2	99.5	95.4	100.5	90.9	100.9	88.3	105.6	97.7	103.1	92.4
October	113.2	103.2	97.3	102.2	95.6	98.9	99.6	93.5	101.4	90.4	101.0	87.8	105.8	97.6	102.6	92.4
November	114.4	103.2	97.3	104.0	95.6	97.8	99.6	94.4	100.8	89.7	100.3	88.4	105.8	96.8	102.3	93.2
December	115.5	102.9	98.5	103.6	95.7	97.1	99.8	93.2	100.4	89.1	100.0	88.9	106.4	95.6	101.4	94.0
1984																
January	116.1	103.5	99.2	105.1	95.4	96.9	100.1	93.1	102.2	88.1	99.1	89.8	106.0	95.4	101.2	95.1
February	114.2	103.3	97.7	107.3	96.5	98.1	100.0	93.1	103.0	88.3	99.3	91.0	104.3	97.0	101.5	94.7
March	112.1	101.1	99.9	107.3	97.7	98.8	100.7	91.8	103.2	88.6	99.7	91.6	103.6	97.1	100.7	95.8
April	113.1	100.9	100.6	105.1	98.0	98.2	101.5	91.0	103.7	88.1	99.2	93.0	103.0	96.6	101.1	96.4